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EFFORTS TO REDUCE TAXPAYER BURDENS

HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT OF THE
INTERNAL REVENUE SERVICE

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

MAY 20, 1983

Printed for the use of the Committee on Finance

U.S. GOVERNMENT PRINTING OFFICE
22-537 O WASHINGTON : 1983

S361-48

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EFFORTS TO REDUCE TAXPAYER BURDENS

FRIDAY, MAY 20, 1983

U.S. SENATE,
SUBCOMMITTEE ON OVERSIGHT OF THE
INTERNAL REVENUE SERVICE,
SENATE COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:40 a.m., in room SD-215, Dirksen Senate Office Building, Honorable Charles E. Grassley (chairman) presiding.

Present: Senators Grassley and Dole.

[The press release announcing the hearing follows:]

[Press release of May 3, 1983, U.S. Senate, Committee on Finance, Subcommittee on Oversight of the Internal Revenue Service]

FINANCE SUBCOMMITTEE ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE SETS HEARINGS ON EFFORTS TO REDUCE TAXPAYER BURDENS

Senator Charles E. Grassley, Chairman of the Subcommittee on Oversight of the Internal Revenue Service of the Senate Committee on Finance, announced today that the Subcommittee will hold a hearing on May 20, 1983 on recent efforts to ease the burden on taxpayers of compliance and further legislative and administrative options to provide additional relief.

The hearings will begin at 9:30 a.m. on May 20, 1983, in SD-215 (formerly Room 2221) of the Dirksen Senate Office Building.

In announcing the hearing, Senator Grassley noted that recent legislation has made important strides toward reducing the burden on honest taxpayers. "The Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) provided important taxpayer protections. The IRS is also making an important contribution to these efforts by its simplification of income tax forms."

Particular areas of concern to the Subcommittee include:

(1) How much progress has the IRS made in reducing the complexity of tax forms and their instructions?

(2) How well has the Paperwork Reduction Act served to stimulate reduced complexity in IRS forms?

(3) Should taxpayer assistance programs be maintained or modified?

(4) Does the IRS provide timely and accurate advice to taxpayers? Can the ruling and regulations process be improved?

(5) Does the current regulations backlog create problems for taxpayers? If so, how is that backlog to be reduced?

(6) Should the IRS explore amnesty arrangements with nonfilers like those adopted by various states to bring such nontaxpayers into the tax system? and

(7) Are the taxpayer safeguard amendments of TEFRA adequate? If not, how may they be improved?

Consolidated testimony.—Senator Grassley urges all witnesses who have a common position or who have the same general interest to consolidate their testimony and designate one person to present their common viewpoint orally to the subcommittee. This procedure will enable the subcommittee to receive a wider expression of views than it might otherwise obtain. Senator Grassley urges that all witnesses exert a maximum effort to consolidate and coordinate their statements.

Legislative Reorganization Act.—Senator Grassley stated that the Legislative Reorganization Act of 1946, as amended, requires all witnesses appearing before the

Committees of Congress "to file in advance written statements of their proposed testimony, and to limit their oral presentations to brief summaries of their argument".

Witnesses scheduled to testify should comply with the following rules:

(1) All witnesses must submit written statements of their testimony.

(2) Written statements must be typed on letter-size paper (not legal size) and at least 100 copies must be delivered not later than noon on Thursday, May 19, 1983.

(3) All witnesses must include with their written statements a summary of the principal points included in the statement.

(4) Oral presentations should be limited to a short discussion of principal points included in the one-page summary. Witnesses must not read their written statements. The entire prepared statement will be included in the record of the hearing.

(5) Not more than 5 minutes will be allowed for the oral summary.

Written statements.—Witnesses who are not scheduled to make an oral presentation, and others who desire to present their views to the subcommittee, are urged to prepare a written statement for submission and inclusion in the printed record of the hearing. These written statements should be typewritten, not more than 25 double-spaced pages in length, and mailed with five (5) copies to Roderick A. DeArment, Chief Counsel, Committee on Finance, Room SD-221, Dirksen Senate Office Building, Washington, D.C. 20510, not later than Friday, June 3, 1983. On the first page of your written statement, please indicate the date and subject of the hearing.

Senator **Grassley**. I would like to call the Subcommittee on Oversight of the IRS hearing to order.

Today our subcommittee will review methods Congress or the IRS can employ to ease the burden on taxpayers attempting to comply with our revenue laws.

The cornerstone of our revenue collection system is voluntary compliance. Taxpayers voluntarily compile their tax returns each year under threat of penalty. The alternative to the present system obviously involves more pressure and involvement of the Government in getting tax information. Encouraging taxpayers to assess themselves correctly, I feel, is the best way to enhance voluntary compliance and to avoid a more totalitarian approach.

I think, without doubt, our country has the highest voluntary compliance of any free society in the world. We want to maintain that. The percentage of compliance has been going down from year to year, and we want to do what we can to improve that. Improving credibility in the tax system is only one of many ways of accomplishing that goal.

To the extent that taxpayers are having difficulty complying with our tax laws, we are creating inconvenience and dissatisfaction among taxpayers and inhibiting the effectiveness of the system to collect revenue.

The subcommittee has chosen a variety of topics which are components of the burden carried by taxpayers in complying with our Federal tax requirements.

The Commissioner of the Internal Revenue Service will address all these topics, and some of our additional witnesses may select a variety of topics for comment.

The IRS has an ongoing review of their forms and instructions. This year the IRS introduced a new form, the 1040-EZ. The EZ is so popular, many of my constituents are complaining that they want to use the new form but are ineligible because they have too much interest, or are married taxpayers.

Not all form simplification is as popular as the 1040-EZ. Some of my constituents have protested the revision of the Employee Business Expense Form 2106 and the proposed revision, schedule F. Practitioners are arguing that these simplifications are reducing the accuracy of the records kept by taxpayers, thereby making the practitioners' task more difficult and increasing the chance of the disallowance of poorly substantiated items on audit.

Closely alined with the form simplification process is the IRS's mandate to comply with the Paperwork Reduction Act. The Paperwork Reduction Act sets goals for the reduction of paperwork generated by each agency. Sometimes the simplification of forms and instructions is necessary to achieve these paperwork goals.

While form and instruction simplification is very desirable, it should not be accomplished at the expense of understandable, clear instructions to taxpayers.

The tension between these goals will be a subject that we will be examining here today. The taxpayer assistance program has been in the center of a budgetary tug-of-war between the Congress and the Department of the Treasury. While Congress has repeatedly appropriated money for this important function, Treasury persists in eliminating taxpayer assistance as a cost-cutting measure. Whether budgetary uncertainty, inadequate funding, or weak administration have caused the current shortcomings of taxpayer service, the source of the problem is an issue which commands congressional attention.

My office, and others throughout the Congress, were deluged with complaints of closures of taxpayer service offices, busy signals on IRS toll-free lines for 1040 filers, and shortages in the supply of necessary forms from local IRS offices. If our goal is to encourage compliance, the absence of effective taxpayer assistance is a great concern to this subcommittee.

A related concern is whether or not the IRS is providing timely and accurate advice to taxpayers. One way in which this advice is disseminated is through the rulings and regulation process. Faced with sweeping Federal legislation in the past 2 years, the IRS has a significant regulation backlog, interpreting new tax legislation. This glut has slowed the review of older regulations.

The absence of a clear IRS position on many issues complicates compliance and creates confusion among practitioners. We must exercise effective oversight over the regulation and ruling process to be sure taxpayers are given sufficient direction to comply with revenue loss.

Now, looking to the future, some taxpayers advocacy groups have suggested that amnesty arrangements with nonfilers be explored to bring more taxpayers into the revenue system. The effectivity of an amnesty program in producing more revenue, and the effect of an amnesty program on the compliance of current compliant taxpayers is another topic which we will be exploring today.

Last year a series of taxpayers' protections were enacted within the Tax Equity and Fiscal Responsibility Act. These provisions have been criticized as being unnecessary by some, and so weak as to be meaningless by others. Perhaps this means that we have struck a proper balance.

But nevertheless, the comments of witnesses on the TEFRA provisions will be helpful to the subcommittee in assessing their effectivity and evaluating possible improvements.

The purpose of this hearing is to investigate the ways to ease taxpayers' burdens. Our efforts here are important in our attempt to increase voluntary compliance and improve taxpayers' attitudes about the fairness of the system. As we enact compliance legislation, it is important to examine whether or not this legislation violates the rights of taxpayers. As more information is gathered by the IRS, issues of taxpayers' privacy become more critical; also, the agency has a greater duty to provide accurate information and helpful advice to taxpayers attempting to comply with this greater burden of Federal regulation.

Before Commissioner Egger offers his views, I would like to take time on behalf of all of us on the subcommittee, as well as, I'm sure, the full committee, to thank Floyd Williams, a staff member on the Joint Committee on Taxation, for his help on many of the hearings of this subcommittee. His hard work and professionalism have been of great assistance to me and my staff during the past 2½ years. Although Republicans always advocate that talented individuals return to the private sector to improve the GNP, I'm going to miss Floyd's assistance. All of us on the subcommittee wish him well in his new endeavors and ask him to continue to give us the benefit of his comments as a practitioner.

At this point, Commissioner Egger is already at the witness table, and he is going to chronicle his agency's achievements in easing taxpayers' burdens. We look forward to hearing suggestions for improvements in the future.

I want to say that I have found Commissioner Egger to be open to dialog about every type of tax administration problem and is willing to discuss the shortcomings of his administration and the system. He is a breath of fresh air in the sense that he is looking for opportunities to achieve exactly what we are discussing today.

I might say that I meet on a fairly regular basis with Commissioner Egger, and that these meetings hopefully increase cooperation between the Congress and the executive branch of Government. It also gives us an opportunity to candidly express our personal concerns and discuss ways to accomplish our mutual goals.

I want to make one announcement prior to your statement, Commissioner Egger, that Senator Dole will probably attend this hearing and chair it from the 10-minute period of time from 10:30 until 10:40. I must absent myself from this subcommittee to help make a quorum on the Subcommittee on Constitution of the Committee on the Judiciary, so that we can pass out of that committee some very important legislation.

Would you proceed, Commissioner Egger?

Commissioner EGGER. I certainly will, Mr. Chairman.

STATEMENT OF HON. ROSCOE L. EGGER, JR., COMMISSIONER, INTERNAL REVENUE SERVICE

Commissioner EGGER. I would like to say a couple of things right at the outset, one of which is that I certainly do share with you the common goal of achieving better compliance in the tax system, and I believe that necessarily involves the integrity of the system and how it is perceived by those of the public who have to share in the annual contribution toward the support of our Government activities.

I would like also to thank you very much for your kind comments. I certainly do want to say, also on the record, that I have had an excellent relationship with you and with this subcommittee, and I believe all to the public good.

Now, I have with me here at the table, Jim Owens, who is the Deputy Commissioner. We also have a number of other Service officials with us, so we believe we will be in a position to answer or to deal with almost any question that you or any of the members may have.

I do have a more complete statement, but for the purposes of getting into the question and answer period I would like to truncate that statement just a bit. So, with your permission, I would like to go ahead and do that.

Senator GRASSLEY. Yes; enter it in the record and summarize; is that what you asked?

Commissioner EGGER. Yes.

Senator GRASSLEY. Yes; that will be granted.

Commissioner EGGER. The size and the complexity of the Internal Revenue Code and the recent volume of tax legislation have kept us busy just trying to keep up to date with new developments; but despite the flurry of activity associated with implementing ERTA and TEFRA, and despite the fact that our efforts will always be viewed by some as being insufficient, we think that significant progress has been made in the last couple of years in simplifying the problems that taxpayers must face in dealing with the tax system of the country.

It is easy to overlook one important fact; that is, that both the taxpayers and the Internal Revenue Service have a keen interest in simplification. To the extent that we can simplify life for taxpayers, we certainly do simplify it for ourselves. For example, if we can somehow reduce the amount of information the taxpayers have to report, or somehow reduce the number of forms necessary for the reporting, we will have eased the burden on both sides of the tax equation. To the extent we can simplify our forms, instructions, and publications to make them more readable and more understandable to a larger portion of the taxpayer population we certainly can hope to reduce the volume of our roughly 47 million taxpayer contacts each year.

My basic point is that the Service has no inherent interest in maintaining complexity in tax administration. Those who suggest, humorously or otherwise, that we do are just wrong, perhaps confused by the obvious difficulties that we often do face in attempting to translate complex legislation into simple procedures for taxpayers to follow. Often this simply can't be done, or it can be done only to a point.

Now let me turn to some of the specific examples that I think show we have tried to make life simpler. One of these is one of the more trying problems that taxpayers face in dealing with the Internal Revenue Service—our lack of responsiveness to correspondence.

Despite improvements made in recent years in reducing the number of complaints, taxpayers and tax practitioners alike continue to find that frequently we just don't act timely or responsively to correspondence, even correspondence seeking explanations of our own letters. Frustrations on this subject, which I experienced myself as a practitioner, were made known to me in the strongest terms by other practitioners, including some friends and former friends, as soon as I became Commissioner.

Because I view this as a serious problem, I asked the Deputy Commissioner to convene a task force of top-level Service executives to determine what steps were necessary to see to it that we improve the situation. The draft version of this report was distributed in-house for comment only last month, and we expect to issue it in final form this summer.

This study contains specific recommendations for improvements in our correspondence policies, procedures, and the letters, the notices, and the forms themselves. For example, we are considering revisions to our correspondence policies to provide firm, realistic response times for replying to taxpayer letters, and replies that specifically reference which items of the letters we are answering—things of that sort. Once implemented, we think the changes that we are considering will be a pleasant surprise for taxpayers as well as tax practitioners, and we think that dealing with the IRS through correspondence hereafter is going to be a lot easier. We are making a major commitment to improving our record in this important area, and I certainly expect visible results.

Perhaps the IRS' most important recent organizational effort to help taxpayers was the creation of the Taxpayer Ombudsman position in my office. Besides representing and advocating taxpayers' rights within the Service, the Ombudsman oversees the IRS' problem resolution program which functions in each of our districts and service centers.

The Ombudsman also reviews IRS policies and procedures for possible adverse effects on taxpayers, proposes ideas to benefit taxpayers, represents taxpayers' views in the design of tax forms and instructions, and suggests changes to proposed or existing legislation, all in the interest of aiding the taxpayers. None of these functions are intended as substitutes for other existing programs, but rather as a means of insuring that these programs work as intended. If they do not, the Ombudsman has the authority to effect changes.

Now, shifting to a slightly different subject, the Chief Counsel's Office has worked with us in seeking to simplify the courtroom aspect of taxpayer contacts with the Service. In June of last year, after consultation with members of the Tax Court as well as numerous private attorneys, Counsel Order No. 4000.6 was issued. This order made revisions to the procedures for Tax Court litigation involving small cases designed to simplify the process for taxpayers representing themselves before the Tax Court. These provisions are significant because taxpayers represent themselves in some 60 percent of these small cases, which involve less than $10,000. As of December 1982, more than 21,000 of these cases were pending in the Tax Court; in addition, of the 31,000 new cases filed with the Tax Court in fiscal year 1982, taxpayers represented themselves in over 16,000 of the cases.

These revised procedures included reducing paperwork by using documents for multiple purposes, increasing the use of oral arguments and decisions, emphasizing the use of plain language in taxpayer correspondence and court documents, and expediting preparation of settlement documents. These changes are benefitting taxpayers, members of the bar and the Tax Court, as well as the IRS, by streamlining the litigation process and by providing much faster resolution of these cases.

We have also made a number of significant strides in simplifying our forms and related items. Let me briefly highlight some of these efforts for you.

Probably the best known new development was the introduction this year of the 1040-EZ form. This form is intended for single taxpayers with one personal exemption, no dependents, and income based on wages, salaries, tips, and no more than $400 in interest.

The 1040-EZ has only 11 lines, 1 of which is already completed for the taxpayer, so that they only have to complete 10 lines—just half as many as the 1040A—and is divided into steps that guide taxpayers through the form. Because of its plain language and new graphic layout, we estimate that completing the 1040-EZ should take less than half the time it takes to complete the 1040A, and only about one-eighth of the time needed for the basic form 1040.

Our statistics to date indicate that the form 1040-EZ has been a success with taxpayers, particularly those who previously used the 1040A. From January 1 to May 14 of this year, nearly 15 million 1040-EZ's were filed, along with nearly 21 million 1040A's. During the same period last year over 37 million 1040A's were filed.

We are developing a new short form, 1120-A. This is a short form for corporations, and we hope to have it in place for possible use by 1985. Introduction of this form could simplify reporting for small corporations by reducing the amount of information required, such as dropping three or four of the schedules, as well as condensing and simplifying the balance sheet information, and by raising the threshhold filing requirements for the submission of more detailed information. We estimate that about 1 million corporate filers will be able to use this new, shorter form.

With regard to simplifying existing forms, our leading effort was the extensive redesign and rewriting of form 1040A and its instructions. This effort began as part of our development of the new form 1040-EZ, and, like the EZ, the 1040A is now designed to guide the taxpayer through the form in a series of clearly marked steps. Each major part of the form is labeled with a step number and heading. Additionally, graphic and typeface changes have improved the appearance of the form and reduced its visual clutter.

Based on our success with the 1040-EZ, we are considering and will soon be testing several more changes to the 1040A for the next filing season. Basically, these center on two different and expanded versions of the 1040A which would draw millions of taxpayers from the longer, more complicated form 1040. Both versions would add child care credits and IRA deductions as well as fully taxable pensions to the 1040A for the first time. One version would also add limited itemized deductions, so many homeowners would be able to switch to the 1040A and still take advantage of itemized deductions.

The result of these tests will help us determine if the potential disadvantages of a slightly longer 1040A form would outweigh the advantages of having fewer taxpayers use the more complex 1040 form.

Finally, Mr. Chairman, you expressed an interest in the extent to which the Paperwork Reduction Act has stimulated reduced complexity in our forms.

The Service had achieved significant taxpayer burden reductions before the act was passed. The act caused us to continue and intensify our efforts to take a close look at the need for information which we ask the taxpayers to supply; but, as I said earlier, the Service believes that simplification works for both taxpayers and the Service, and both of those reasons have been ample incentive for the IRS to do more in simplification.

The improvements we are seeing now in the 1040-EZ and the 1040A had their beginnings before the act was passed, and I think are a tribute to the continuing commitment of the IRS to make progress in form simplification. We believe this commitment has resulted in many more taxpayers being able to prepare their own tax returns. In fact, over the past 5 years the percentage of tax returns completed by paid preparers has declined from 43 to 37 percent.

Now, just as our efforts to improve taxpayer-IRS contacts and to simplify our forms and publications provide benefits to all taxpayers, so do our efforts to simplify the rulings and regulations processes. It is through these mechanisms that we provide technical guidance to taxpayers and their representatives.

We believe expanded use of the "safe harbor" approach to substantiation of items claimed on the return has the potential to be a major advance in the regulations and rulings area. While this is not a new concept, the approach provides previously untapped possibilities for simplifying tax administration. It offers benefits to the taxpayer, who has reduced paperwork and recordkeeping requirements while using it, as well as the Service, which has fewer issues to consider in processing and examining the returns. Perhaps the leading example of this to date is the proposed regulation, which is outstanding now, establishing a standard rate for meal expenses for the millions of taxpayers who make their living traveling. They may elect to use this standard safe-harbor rate without substantiation, or to continue to substantiate actual amounts if they are in excess of the standard rate. We are now looking at other areas to see if they, too, have potential for this kind of safe-harbor approach.

Mr. Chairman, I understand you are interested in exploring the issue of amnesty for nonfilers as a way of bringing them back into the system. Before going into the details of this issue, though, I would like to briefly define what the Service means when we talk about amnesty.

To us, amnesty means forgiveness from criminal prosecution only, and has no effect on the imposition of civil tax penalties or the collection of tax, or the collection of interest. Even under this definition, however, amnesty would be available only under certain conditions such as the absence of any Service investigation of that taxpayer beforehand.

Let me give you a brief summary of this issue in IRS as background for our current position. Starting around 1934 and going until 1951, the Service followed the general practice of not recommending prosecution in cases where taxpayers made voluntary disclosures before investigations had been initiated. In 1952, this practice was officially abandoned because of severe administrative difficulties; for example, some taxpayers who had received immunity subsequently defaulted on their liabilities and then could not be prosecuted.

In 1961, as a part of the servicewide installation of data processing, a news release was issued suggesting that this was a good time for voluntary disclosures and, without promising anything, noted that the likelihood of prosecution was not high in such cases. Policy statement P-9-2, entitled "Prosecution of Criminal Investigation Cases," includes voluntary disclosure as one of the criterion that we use in determining whether a case warrants criminal prosecution.

Amnesty does offer the potential benefit of bringing nonfilers into the system, as you mentioned. There are, however, a number of serious drawbacks to the idea. For example, honest taxpayers may perceive an amnesty as "special treatment" for dishonest taxpayers, and therefore unfair, inequitable, and contrary to IRS policy of administering the laws on a uniform basis. Moreover, instituting one amnesty might encourage the belief that the offer would be repeated in the future, leading to noncompliance in the interim. Finally, the administrative difficulties encountered earlier are likely to reappear, making implementation very difficult.

While we are aware that interest in this idea seems to be increasing, and certainly we are not closing our minds to the idea; nonetheless, at this particular time, based on everything we know, the idea does not appear to warrant any immediate implementation.

You also expressed an interest in the adequacy of the taxpayer safeguard provisions in TEFRA and whether or not they needed improvement. As you may recall, the Internal Revenue Service participated very early on in the drafting and working with those provisions in the bills that were developed here in the Senate Finance Committee, and we supported them throughout debate on the bill.

However, it is still too early to tell with any certainty whether these provisions are working as intended. We need a little more operational experience with TEFRA overall before we will be in a position to determine whether the safeguards are fully adequate. You may be assured that we will keep the Congress and this subcommittee advised if we find that additional legislative measures are going to be necessary.

Mr. Chairman, I have attempted to highlight in this oral statement a few of the most significant efforts that the IRS has made recently to simplify life for taxpayers. There are many other examples which I have not included here, in the interests of brevity.

Some of our work began as efforts at internal efficiency and productivity, which also provided taxpayer benefits as a byproduct. Other advances were conceived and developed exclusively for the taxpayers' benefit. But the common thread in either case is our desire to do our job, which by definition includes both internal efficiency and increasing simplicity for taxpayers better. We are constantly striving to improve in both aspects of our job in order to make the "service" in Internal Revenue Service more than just an empty word.

Mr. Chairman, my associates and I would be pleased to answer any questions that you or members of the subcommittee may have.

[Commissioner Egger's prepared statement follows:]

OPENING STATEMENT
ROSCOE L. EGGER, JR.
COMMISSIONER OF INTERNAL REVENUE
BEFORE THE
SUBCOMMITTEE ON OVERSIGHT OF THE IRS
SENATE FINANCE COMMITTEE

MAY 20, 1983

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE:

I AM PLEASED TO BE WITH YOU TODAY TO DISCUSS THE SERVICE'S EFFORTS TO SIMPLIFY LIFE FOR TAXPAYERS IN DEALING WITH THE TAX ADMINISTRATION SYSTEM. IN MY TESTIMONY, I WILL PROVIDE AN OVERVIEW OF OUR CONTINUING EFFORTS IN THIS AREA AND HIGHLIGHT SEVERAL SPECIFIC PROJECTS I BELIEVE ARE OF PARTICULAR INTEREST.

WITH ME TODAY ARE JIM OWENS, THE DEPUTY COMMISSIONER, AND A NUMBER OF OTHER SERVICE OFFICIALS REPRESENTING THE MAJOR FUNCTIONAL AREAS TO BE COVERED IN MY STATEMENT. WE WILL BE AVAILABLE TO ANSWER ANY QUESTIONS YOU OR THE MEMBERS MAY HAVE AT THE CONCLUSION OF MY TESTIMONY.

IRS EFFORTS TO SIMPLIFY LIFE FOR TAXPAYERS

THE SIZE AND COMPLEXITY OF THE INTERNAL REVENUE CODE AND THE RECENT VOLUME OF TAX LEGISLATION HAVE KEPT US BUSY JUST TRYING TO KEEP UP WITH THESE NEW DEVELOPMENTS. DESPITE THE

FLURRY OF ACTIVITY ASSOCIATED WITH IMPLEMENTING ERTA AND TEFRA, AND DESPITE THE FACT THAT OUR EFFORTS WILL ALWAYS BE VIEWED BY SOME AS INSUFFICIENT, WE BELIEVE SIGNIFICANT PROGRESS HAS BEEN MADE IN THE PAST COUPLE OF YEARS IN SIMPLIFYING THE PROBLEMS TAXPAYERS FACE IN DEALING WITH THE TAX ADMINISTRATION SYSTEM.

IT IS EASY TO OVERLOOK ONE IMPORTANT FACT HERE -- BOTH TAXPAYERS AND THE SERVICE HAVE AN INTEREST IN SIMPLIFICATION. TO THE EXTENT THAT WE CAN SIMPLIFY LIFE FOR TAXPAYERS, WE ALSO SIMPLIFY IT FOR OURSELVES. FOR EXAMPLE, IF WE CAN SOMEHOW REDUCE THE AMOUNT OF INFORMATION TAXPAYERS HAVE TO REPORT, OR SOMEHOW REDUCE THE NUMBER OF FORMS NECESSARY FOR THE REPORTING OF THAT INFORMATION, WE WILL HAVE EASED THE BURDEN ON BOTH SIDES OF THE TAX "EQUATION." OR, TO THE EXTENT WE CAN SIMPLIFY OUR FORMS, INSTRUCTIONS, AND PUBLICATIONS TO MAKE THEM MORE UNDERSTANDABLE TO A LARGER PORTION OF THE TAXPAYER POPULATION, WE MAY REDUCE THE VOLUME OF OUR 47 MILLION PLUS TAXPAYER CONTACTS A YEAR.

MY BASIC POINT IS THAT THE SERVICE HAS NO INHERENT INTEREST IN MAINTAINING COMPLEXITY IN TAX ADMINISTRATION. THOSE WHO SUGGEST -- HUMOROUSLY OR OTHERWISE -- THAT WE DO ARE WRONG, PERHAPS CONFUSED BY THE OBVIOUS DIFFICULTIES WE OFTEN FACE IN "TRANSLATING" COMPLEX LEGISLATION INTO SIMPLE PROCEDURES FOR

TAXPAYERS. OFTEN THIS CANNOT BE DONE, OR CAN BE DONE ONLY TO A POINT.

LET ME NOW TURN TO SOME SPECIFIC EXAMPLES OF OUR EFFORTS TO MAKE LIFE SIMPLER FOR TAXPAYERS. FOR CONVENIENCE, WE HAVE ORGANIZED THESE EXAMPLES UNDER THREE BROAD HEADINGS WHICH WE FEEL REPRESENT THE MAJOR INITIATIVES UNDERWAY: DIRECT TAXPAYER CONTACTS, TAX FORMS AND PUBLICATIONS, AND RULINGS AND REGULATIONS.

1. DIRECT TAXPAYER CONTACTS

ONE OF THE MORE TRYING PROBLEMS TAXPAYERS FACE IN DEALING WITH IRS IS OUR LACK OF RESPONSIVENESS TO CORRESPONDENCE. DESPITE IMPROVEMENTS MADE IN RECENT YEARS IN REDUCING THE NUMBER OF COMPLAINTS, TAXPAYERS AND TAX PRACTITIONERS ALIKE CONTINUE TO FIND THAT IRS DOES NOT ACT TIMELY OR RESPONSIVELY TO CORRESPONDENCE -- EVEN CORRESPONDENCE SEEKING EXPLANATIONS OF OUR OWN LETTERS. FRUSTRATIONS ON THIS SUBJECT, WHICH I HAD EXPERIENCED MYSELF AS A PRACTITIONER, WERE MADE KNOWN TO ME IN THE STRONGEST TERMS BY OTHER PRACTITIONERS AS SOON AS I BECAME COMMISSIONER.

Because I view this as a serious problem, I directed the Deputy Commissioner to convene a task force of top-level Service executives to determine what steps were necessary to improve the situation. The draft version of their report was distributed internally for comments last month, and should be issued in final form this summer.

The study contains specific recommendations for improvements in our correspondence policies, procedures, and the letters, notices, and forms themselves. For example, we are considering revisions to our correspondence policies to provide firm, realistic response times for replying to taxpayer letters, and replies that specifically reference which item(s) from the letters we are answering. Operating procedures in all Service functions will be reviewed in order to find ways to place increased emphasis on handling taxpayer correspondence, including such possible changes as telling taxpayers exactly when we will respond to them, and then controlling and processing the correspondence in such a way that we can meet those dates. Our letters, notices, and forms will be scrutinized for ways to provide taxpayers more specific guidance on information we are seeking, as well as to keep them better advised of our procedures for resolving their problems.

Once implemented, we believe the changes we are considering will be a pleasant surprise for taxpayers and tax practitioners alike, and will make dealing with the IRS through correspondence an easier job. We are making a major commitment to improving our record in this important area, and expect visible results.

Perhaps IRS' most important recent organizational effort to help taxpayers was the creation of the Taxpayer Ombudsman position in my office. Besides representing and advocating taxpayers' rights within the Service, the Ombudsman oversees the IRS' Problem Resolution Program (PRP), which functions in each of our districts and service centers.

The Ombudsman also reviews IRS policies and procedures for possible adverse effects on taxpayers, proposes ideas to benefit taxpayers, represents taxpayers' views in the design of tax forms and instructions, and suggests changes to proposed or existing legislation to aid taxpayers. None of these functions are intended as substitutes for other existing programs, but rather as a means of insuring that these programs work as intended. If they do not, the Ombudsman can effect changes.

OUR TAXPAYER SERVICE PROGRAM IS ANOTHER ORGANIZATIONAL EFFORT TO AID TAXPAYERS IN THEIR DEALINGS WITH THE IRS. AS YOU WELL KNOW, MR. CHAIRMAN, THIS PROGRAM HAS BEEN THE FOCUS OF INTENSE DEBATE RECENTLY. BECAUSE OF THE EFFORTS OF MANY IN THE CONGRESS, INCLUDING YOURSELF, TAXPAYERS ARE RECEIVING THE SAME LEVEL OF TAX ASSISTANCE IN FY 1983 AS LAST YEAR. WE SHARE YOUR CONCERN OVER THE NEED TO HELP TAXPAYERS MEET THEIR FILING RESPONSIBILITIES AND RESOLVE THEIR TAX ACCOUNT PROBLEMS, AND WILL CONTINUE TO SEEK THE MOST COST-EFFECTIVE WAYS TO PROVIDE THESE VITAL SERVICES.

IN FISCAL YEAR 1982, IRS RECEIVED OVER 170 MILLION RETURNS AND RELATED DOCUMENTS FOR PROCESSING. THE SHEER VOLUME OF PAPER AND INFORMATION WE RECEIVE MAKES IT DIFFICULT TO ANSWER QUESTIONS ON SPECIFIC TAXPAYER ACCOUNTS IN A TIMELY WAY. BECAUSE OF THIS, THE SERVICE IS EVER MINDFUL OF THE VALUE OF AUTOMATION IN HELPING US MORE EFFICIENTLY DEAL WITH TAXPAYERS. ONE MAJOR INITIATIVE IN THIS AREA IS THE IMPLEMENTATION OF OUR MICROFILM REPLACEMENT SYSTEM (MRS), WHICH SPEEDS THE PROVISION OF INFORMATION TO EMPLOYEES RESPONDING TO TAXPAYERS' QUESTIONS ON THEIR ACCOUNTS. RESEARCH WHICH PREVIOUSLY REQUIRED TWO WEEKS CAN NOW BE COMPLETED IN 24 HOURS, ALLOWING US TO GIVE TAXPAYERS THE VERY LATEST INFORMATION ON THEIR ACCOUNTS, BE MORE ACCURATE

AND TIMELY IN REPLYING TO CORRESPONDENCE, ETC. CONSIDERING THAT THE SERVICE RECEIVED NEARLY 16 MILLION INQUIRIES IN FY 1982 WHICH REQUIRED MICROFILM RESEARCH, THE MAGNITUDE OF IMPROVEMENT IN THIS AREA BECOMES CLEAR. ALL OF OUR SERVICE CENTERS AND ASSOCIATED DISTRICT OFFICES HAVE CONVERTED TO MRS EXCEPT CINCINNATI, WHICH DOES SO NEXT MONDAY, THE 23RD.

THE CHIEF COUNSEL'S OFFICE HAS SOUGHT TO SIMPLIFY THE COURTROOM ASPECTS OF TAXPAYER CONTACTS WITH IRS. IN JUNE OF 1982, AFTER CONSULTATION WITH MEMBERS OF THE TAX COURT AND PRIVATE ATTORNEYS, COUNSEL ORDER 4000.6 WAS ISSUED. IT MADE REVISIONS TO THE PROCEDURES FOR TAX COURT LITIGATION INVOLVING SMALL CASES DESIGNED TO SIMPLIFY THE PROCESS FOR TAXPAYERS REPRESENTING THEMSELVES BEFORE THE TAX COURT. THESE PROVISIONS ARE SIGNIFICANT BECAUSE TAXPAYERS REPRESENT THEMSELVES IN SOME 60% OF THESE SMALL CASES, WHICH INVOLVE LESS THAN $10,000. AS OF DECEMBER 1982, OVER 21,000 OF THESE CASES WERE PENDING IN THE TAX COURT. IN ADDITION, OF THE 31,000 NEW CASES FILED WITH THE TAX COURT IN FY 1982, TAXPAYERS REPRESENTED THEMSELVES IN OVER 16,000.

THESE REVISED PROCEDURES INCLUDED REDUCING PAPERWORK BY USING DOCUMENTS FOR MULTIPLE PURPOSES; INCREASING THE

USE OF ORAL ARGUMENTS AND DECISIONS (AUTHORIZED BY THE MISCELLANEOUS REVENUE ACT OF 1982); EMPHASIZING THE USE OF PLAIN LANGUAGE IN TAXPAYER CORRESPONDENCE AND COURT DOCUMENTS; AND EXPEDITING PREPARATION OF SETTLEMENT DOCUMENTS. THESE CHANGES ARE BENEFITTING TAXPAYERS, MEMBERS OF THE BAR AND THE TAX COURT, AND IRS ALIKE BY STREAMLINING THE LITIGATION PROCESS AND BY PROVIDING MUCH FASTER RESOLUTION OF THESE CASES.

2. TAX FORMS AND PUBLICATIONS

THE PROBLEMS TAXPAYERS FACE IN DEALING WITH IRS ARE OFTEN DIRECTLY RELATED TO OUR MANY FORMS, INSTRUCTIONS, AND PUBLICATIONS. THE COMPLEXITY OF THESE DOCUMENTS IS THE RESULT OF TWO MAJOR FACTORS: THE DIFFICULTIES INHERENT IN TRANSLATING COMPLEX LEGISLATION INTO SIMPLE PROCEDURES, WHICH I NOTED EARLIER; AND THE REQUIREMENTS TO GATHER CERTAIN INFORMATION FROM TAXPAYERS TO PROPERLY IMPLEMENT THE LAWS.

HOWEVER, WE HAVE MADE A NUMBER OF SIGNIFICANT STRIDES IN THIS AREA TO SIMPLIFY THE FORMS AND RELATED ITEMS, AND TO MAKE THEM AVAILABLE THROUGH A WIDER VARIETY OF CHANNELS. LET ME BRIEFLY HIGHLIGHT SOME OF THESE EFFORTS FOR YOU.

IN AN EFFORT TO GIVE OUR FORMS, INSTRUCTIONS, AND PUBLICATIONS THE WIDEST POSSIBLE DISTRIBUTION THIS YEAR, WE USED A NETWORK OF OVER 55,000 PUBLIC OUTLETS SERVING AS DISTRIBUTION POINTS FOR IRS TAX MATERIALS. THESE OUTLETS MADE AVAILABLE TO INDIVIDUAL FILERS OVER 1.5 BILLION FORMS AND OVER 45 MILLION INSTRUCTION BOOKLETS, TAX GUIDES AND SPECIALIZED INFORMATION PUBLICATIONS -- ALL IN ADDITION TO THE ANNUAL MAILOUT OF OVER 90 MILLION TAX PACKAGES.

IRS ADDED 8,200 FORMS OUTLETS IN 1983, AND MOST OF THIS INCREASE IS TIED EXCLUSIVELY TO THE VOLUNTARY EFFORTS OF PUBLIC AND COLLEGE LIBRARIANS. MANY OF THE COUNTRY'S LARGEST LIBRARY SYSTEMS ARE STOCKING BULK SUPPLIES OF MAJOR IRS TAX FORMS AND MAINTAINING A FILE OF REPRODUCIBLE MASTER COPIES OF MANY OF THE LESSER-USED FORMS. THEY HAVE CREATED REFERENCE SECTIONS FOR OUR INFORMATION PUBLICATIONS AND ADDED AUDIO CASSETTES ON THE PREPARATION OF TAX RETURNS AS PART OF THEIR MULTI-MEDIA PROGRAMS. IN ADDITION, THEY DISSEMINATE ON OUR BEHALF BROCHURES AND PROMOTIONAL MATERIAL ON SUCH IRS PROGRAMS AS TELE-TAX, TAX DIAL, TOLL-FREE, VITA, TCE, AND MANY OF THE ALTERNATIVE IRS PROGRAMS AVAILABLE FOR OBTAINING TAX MATERIAL OR TAX ASSISTANCE. OVER 18,000 LIBRARIES ACROSS THE COUNTRY PERFORMED AT LEAST ONE OF THESE FUNCTIONS LAST YEAR.

To make Members of Congress aware of the services we offer taxpayers in this area, I wrote each Member of Congress on March 11 of this year to point out the specific ways constituents could receive forms and publications in that district or state. This letter included appropriate phone numbers and addresses for the Member, and was in addition to my January 11 letter to all Members, which provided sample copies of Publications 17, 334, 225, and 910, our principle publications for assisting individual taxpayers. We understand this information has been extremely helpful to Congressional staffers who handle constitutent inquiries in this area.

Our improvement efforts on specific tax forms and publications could be divided into three groups: new developments, simplification, and consolidation.

Perhaps our best-known new development was the introduction of the Form 1040EZ for 1982. This form is intended for single taxpayers with one personal exemption, no dependents, and income based on wages, salaries, tips, and no more than $400 in interest.

The 1040EZ has only 11 lines, half as many of the 1040A, and is divided into steps that guide taxpayers through the form. Because of its plain language and new graphic layout, we estimate that completing the 1040EZ should take less than half the time it takes to complete the Form 1040A, and only about one-eighth the time needed for the basic Form 1040, without attached schedules.

Our statistics to date indicate that the Form 1040EZ has been a success with taxpayers, particularly those who previously used the 1040A. Between January 1-May 14 of this year, nearly 15 million 1040EZ's were filed, along with nearly 21 million 1040A's. During the same period last year, over 37 million 1040A's were filed.

Besides simplifying filing requirements for almost 15 million taxpayers, the introduction of the 1040EZ will save IRS up to half a million dollars in processing costs annually -- a perfect example of simplification working for the taxpayer and the IRS, as I mentioned earlier.

Another new development this year was Publication 910, "Taxpayer's Guide to IRS Information and Assistance", which as I mentioned was sent to each Member of Congress in

JANUARY. THIS VALUABLE REFERENCE PROVIDES AN OVERVIEW OF THE MAJOR IRS SERVICES AVAILABLE TO TAXPAYERS, AND SHOWS THEM WHERE TO FIND ADDITIONAL HELP IF NEEDED. INFORMATION ON OUR MAJOR PUBLICATIONS IS ALSO INCLUDED.

IN THE EMPLOYEE PLANS AREA, TWO NEW SHORT FORMS (5307 AND 6406) WERE DEVELOPED FOR REQUESTING DETERMINATION LETTERS ON PLAN AMENDMENTS FOR PREVIOUSLY-APPROVED PLANS AND FOR DETERMINATION LETTERS FOR MASTER OR PROTOTYPE PLANS. THIS SIMPLIFIED METHOD RELIEVES PRACTITIONERS FROM PROVIDING UNNECESSARY INFORMATION, WHILE AT THE SAME TIME ALLOWING THE SERVICE TO EXPEDITE A DECISION WITHOUT RESEARCHING THE ORIGINAL PLAN APPROVED.

FINALLY, WE ARE DEVELOPING A FORM 1120-A, U.S. SHORT FORM CORPORATION TAX RETURN, FOR POSSIBLE USE IN 1985. INTRODUCTION OF THIS FORM COULD SIMPLIFY REPORTING FOR SMALL CORPORATIONS BY REDUCING THE AMOUNT OF INFORMATION REQUIRED (SUCH AS DROPPING SCHEDULES A, C, E, AND F, AS WELL AS SIMPLIFYING THE BALANCE SHEETS) AND BY RAISING THE THRESHHOLD FILING REQUIREMENTS FOR THE SUBMISSION OF MORE DETAILED INFORMATION. WE ESTIMATE THAT ABOUT ONE MILLION CORPORATE FILERS WOULD BE ABLE TO USE THIS NEW, SHORTER FORM.

WITH REGARD TO SIMPLIFICATION, OUR LEADING EFFORT WAS THE EXTENSIVE REDESIGN AND REWRITING OF FORM 1040A AND ITS INSTRUCTIONS. THIS EFFORT BEGAN AS PART OF OUR DEVELOPMENT OF THE NEW FORM 1040EZ; LIKE THE 1040EZ, THE 1040A NOW IS DESIGNED TO GUIDE THE TAXPAYER THROUGH THE FORM IN A SERIES OF CLEARLY-MARKED STEPS. EACH MAJOR PART OF THE FORM IS LABELED WITH A STEP NUMBER AND HEADING. ADDITIONALLY, GRAPHIC AND TYPEFACE CHANGES HAVE IMPROVED THE APPEARANCE OF THE FORM AND REDUCED ITS VISUAL CLUTTER.

THE 1040A INSTRUCTIONS WERE REWRITTEN TO PARALLEL THE NEW STEPS ON THE FORM. THEY TOO WERE SET IN NEW TYPEFACE, AND USED A ONE-COLUMN FORMAT WITH A WIDE LEFT MARGIN THAT INCLUDED "TAX TIPS" -- NOTES ABOUT BENEFITS THAT TAXPAYERS MIGHT NOT BE AWARE OF OTHERWISE. WORKSHEETS WERE ALSO REDESIGNED, AND EXAMPLES IMPROVED AND EXPANDED.

BASED ON OUR SUCCESSES WITH THE 1040EZ, WE ARE CONSIDERING -- AND WILL SOON BE TESTING -- SEVERAL MORE CHANGES TO THE 1040A FOR THE NEXT FILING SEASON. BASICALLY, THESE CENTER ON TWO DIFFERENT AND EXPANDED VERSIONS OF THE 1040A THAT SHOULD DRAW MILLIONS OF TAXPAYERS FROM THE LONGER, MORE COMPLICATED FORM 1040. BOTH VERSIONS WOULD ADD CHILD CARE CREDITS, IRA DEDUCTIONS, AND FULLY TAXABLE PENSIONS TO THE 1040A FOR THE FIRST

TIME. ONE VERSION WOULD ALSO ADD LIMITED ITEMIZED DEDUCTIONS, SO MANY HOMEOWNERS WOULD BE ABLE TO SWITCH TO THE 1040A AND STILL TAKE ADVANTAGE OF ITEMIZED DEDUCTIONS.

THE RESULT OF THESE TESTS WILL HELP US DETERMINE IF THE POTENTIAL DISADVANTAGES OF A SLIGHTLY LONGER 1040A WOULD OUTWEIGH THE ADVANTAGES OF HAVING FEWER TAXPAYERS USE THE MORE COMPLEX 1040.

WE HAVE ALSO DEVELOPED A SIMPLIFIED ONE-PAGE VERSION OF FORM 2106, EMPLOYEE BUSINESS EXPENSES, BY ELIMINATING A NUMBER OF ITEMS AND CONDENSING OTHERS. WE ELIMINATED THE DEPRECIATION SCHEDULE ON FORM 2106 AND REDUCED SUBSTANTIALLY THE DETAIL OF INFORMATION REQUIRED TO SUPPORT DEDUCTIONS FOR AUTOMOBILE EXPENSES. ALSO, WE NOW REQUEST ONLY THE MOST IMPORTANT INFORMATION REGARDING DEDUCTIONS FOR EDUCATIONAL EXPENSES. OUR INTENT TO REQUEST LESS INFORMATION WHEREVER POSSIBLE HAS ALSO BEEN REFLECTED IN SIMILAR BURDEN REDUCTION EFFORTS ON FORM 1040: SCHEDULE C, PROFIT (OR LOSS) FROM BUSINESS OR PROFESSION; SCHEDULE D, CAPITAL GAINS AND LOSSES; SCHEDULE E, SUPPLEMENTAL INCOME SCHEDULE; SCHEDULE G, INCOME AVERAGING; AND SCHEDULE SE, COMPUTATION OF SOCIAL SECURITY SELF-EMPLOYMENT TAX.

In the Employee Plans area, filing requirements for Form 5500G were eliminated for governments and most churches, and Form 5310 was revised to satisfy both IRS and PBGC filing requirements for a plan termination, thus providing "one stop service" for taxpayers.

In Exempt Organizations, revisions to Form 990 raised the filing threshhold (relieving some 16% of all 1981 filers from filing in 1982), simplified recordkeeping requirements along lines adopted by the AICPA, and made the form acceptable to 31 states and the District of Columbia for their reporting needs. These states have jurisdiction over about 96% of the charities which formerly had to file one or more state forms. Both the Treasury Department and OMB have approved the establishment of a "Form 990 Committee" to continue improvements in this area.

Publications 568A and 594, both on "The Collection Process", were revised to provide individual and business taxpayers with an easier to understand, more concise version covering their rights and duties in the tax administration system.

Our efforts at consolidation have resulted in the reduction of the "families" of Forms 1087 and 1099, and Form 4347, from a total of twenty forms to nine. Further, our new Form 5471, "Information Return with Respect to Foreign Corporation," replaces five separate forms previously used to obtain the same information.

Finally, Mr. Chairman, you expressed an interest in the extent to which the Paperwork Reduction Act has stimulated reduced complexity in our Forms. The Service had achieved significant burden reductions before the Act was passed. The Act caused us to continue and intensify our earlier efforts to take a close and hard look at our need for the information we ask taxpayers to supply. As I said earlier, the Service believes that simplification works for both taxpayers and the Service, and both of those reasons have been ample incentive for IRS to do more in simplification. The improvements we are seeing now in the 1040EZ and 1040A had their beginnings before the Act was passed, and are a tribute to our continuing commitment to progress in tax forms simplification. We believe that this commitment has resulted in many more taxpayers being able to prepare their own tax returns. In fact, over the past five years, the percentage of tax returns completed by paid preparers has declined from 43% to 37%.

3. RULINGS AND REGULATIONS

JUST AS OUR EFFORTS TO IMPROVE TAXPAYER-IRS CONTACTS AND SIMPLY OUR FORMS AND PUBLICATIONS PROVIDE BENEFITS TO ALL TAXPAYERS, SO DO OUR EFFORTS TO SIMPLIFY THE RULINGS AND REGULATIONS PROCESSES. IT IS THROUGH THESE MECHANISMS THAT WE PROVIDE TECHNICAL GUIDANCE TO TAXPAYERS AND THEIR REPRESENTATIVES.

WE BELIEVE EXPANDED USE OF THE "SAFE HARBOR" APPROACH TO SUBSTANTIATION OF ITEMS CLAIMED ON THE RETURN HAS THE POTENTIAL TO BE A MAJOR ADVANCE IN THE REGULATIONS AND RULINGS AREA. WHILE NOT NEW, THIS APPROACH PROVIDES PREVIOUSLY UNTAPPED POSSIBLITIES FOR SIMPLIFYING TAX ADMINISTRATION. IT OFFERS BENEFITS TO THE TAXPAYER, WHO HAS REDUCED PAPERWORK AND RECORDKEEPING REQUIREMENTS WHILE USING IT, AS WELL AS THE SERVICE, WHICH HAS FEWER ISSUES TO CONSIDER IN PROCESSING AND EXAMINING RETURNS. PERHAPS THE LEADING EXAMPLE OF THIS TO DATE IS THE PROPOSED REGULATION ESTABLISHING A STANDARD RATE FOR MEAL EXPENSES FOR TAXPAYERS WHO ARE TRAVELLING. THEY MAY ELECT TO USE THIS STANDARD "SAFE HARBOR" RATE WITHOUT SUBSTANTIATION, OR TO CONTINUE TO SUBSTANTIATE ACTUAL AMOUNTS IF IN EXCESS OF THE STANDARD RATE. WE ARE NOW LOOKING AT OTHER AREAS TO SEE IF THEY TOO HAVE POTENTIAL FOR THE SAFE HARBOR APPROACH.

IN COOPERATION WITH THE DEPARTMENT OF THE TREASURY, WE HAVE MADE A SIGNIFICANT EFFORT TO EXPEDITE THE REGULATIONS REVIEW PROCESS. THE SYSTEM WE HAVE DEVELOPED ENABLES US TO FOCUS ON THE MORE SIGNIFICANT REGULATIONS AND TO REDUCE THE TIME REQUIRED FOR TREASURY REVIEW OF ROUTINE REGULATIONS, BOTH OF WHICH PROMOTE PROMPTER PUBLICATION.

THIS EFFORT TO EXPEDITE THE REVIEW PROCESS HAS THREE MAJOR ELEMENTS. THE FIRST IS THE USE OF A THREE-TIER CLASSIFICATION SYSTEM. UNDER IT, ALL REGULATIONS PROJECTS ARE ASSIGNED EITHER A CATEGORY III (SIGNIFICANT POLICY ISSUES), CATEGORY II (SOME POLICY ISSUES BUT LARGELY INTERPRETATIVE AND TECHNICAL), OR CATEGORY I (NO POLICY ISSUES, BUT IMPORTANT TO ADMINISTRATION OF THE TAX SYSTEM) RANKING.

THE SECOND ELEMENT IS THE USE OF GOALS FOR THE NUMBER OF PROJECTS TO BE TRANSMITTED MONTHLY TO THE STAFFS AT THE TREASURY DEPARTMENT. IN ADDITION, THE TRANSMISSION DATES FOR THESE PROJECTS ARE SCHEDULED UP TO A YEAR IN ADVANCE WHEREVER POSSIBLE.

THE THIRD ELEMENT IS THE REVISION OF CHIEF COUNSEL'S INTERNAL PROCEDURES, WHICH NOW FEATURE A COORDINATED PROCESS ALLOWING FOR THE TIMELY REVIEW AND APPROVAL OF PROJECTS BY THE CHIEF COUNSEL REVIEW GROUP. A MEMBER OF MY IMMEDIATE STAFF IS A DELEGATE TO THE GROUP.

THESE EFFORTS HAVE PAID OFF IN BETTER USE OF OUR CHIEF COUNSEL RESOURCES AND A MORE EFFECTIVE USE OF TREASURY STAFF'S TIME. WHILE OUR BACKLOG OF REGULATIONS PROJECTS IS STILL EXTENSIVE, PROGRESS IS BEING MADE, AND WE ANTICIPATE EVEN GREATER PROGRESS AS OUR EXPERIENCE WITH THIS NEW SYSTEM INCREASES. BOTH BNA'S "DAILY TAX REPORT" AND CCH'S "TAXES ON PARADE" HAVE NOTED THE RECENT IMPROVEMENTS IN THIS AREA.

REVENUE PROCEDURE 82-51 WAS A MAJOR DEVELOPMENT IN ALLOWING TAXPAYERS UNDER EXAMINATION TO PRE-PAY THEIR TAX LIABILITIES WHILE RETAINING THEIR APPEAL RIGHTS. THE ADVANTAGE TO TAXPAYERS IS THAT SUCH PRE-PAYMENT STOPS THE RUNNING OF INTEREST ON UNASSESSED DEFICIENCIES, YET PRESERVES THE RIGHT TO CONTEST THE SAME LIABILITY IN THE TAX COURT.

FINALLY, A SERIES OF REVENUE PROCEDURES HAVE ELIMINATED THE NEED FOR TAXPAYERS TO APPLY AND RECEIVE PERMISSION FOR THE ADOPTION OF, OR A CHANGE IN, ACCOUNTING PERIODS OR METHODS. THIS "AUTOMATIC CONSENT" APPROACH SAVES TIME AND PAPERWORK FOR BOTH TAXPAYERS AND THE SERVICE.

THE ISSUE OF AMNESTY

I UNDERSTAND YOU ARE INTERESTED IN EXPLORING THE ISSUE OF AMNESTY FOR NON-FILERS, AS A WAY OF BRINGING THEM BACK INTO THE TAX ADMINISTRATION SYSTEM. BEFORE GOING INTO THE DETAILS OF THIS ISSUE, I'D LIKE TO BRIEFLY DEFINE WHAT THE SERVICE MEANS WHEN WE SPEAK OF AN AMNESTY. TO US, AMNESTY MEANS FORGIVENESS FROM CRIMINAL PROSECUTION ONLY, AND HAS NO EFFECT ON THE IMPOSITION OF CIVIL TAX PENALTIES OR THE COLLECTION OF TAX, PENALTIES, AND INTEREST. EVEN UNDER THIS DEFINITION, AMNESTY WOULD BE AVAILABLE ONLY UNDER CERTAIN CONDITIONS, SUCH AS THE ABSENCE OF ANY SERVICE INVESTIGATION OF THAT TAXPAYER.

LET ME GIVE YOU A BRIEF SUMMARY OF THE HISTORY OF THIS ISSUE IN IRS AS BACKGROUND FOR OUR CURRENT POSITION ON IT. FROM 1934 TO 1951, THE SERVICE FOLLOWED A GENERAL PRACTICE OF NOT RECOMMENDING PROSECUTION IN CASES WHERE TAXPAYERS MADE VOLUNTARY DISCLOSURES BEFORE INVESTIGATIONS HAD BEEN INITIATED. IN 1952, THIS PRACTICE WAS OFFICIALLY ABANDONED BECAUSE OF ADMINISTRATIVE DIFFICULTIES; E.G., SOME TAXPAYERS WHO HAD RECEIVED IMMUNITY SUBSEQUENTLY DEFAULTED ON THEIR LIABILITIES AND COULD NOT BE PROSECUTED. IN 1961, AS PART OF THE SERVICEWIDE INSTALLATION OF DATA PROCESSING, A NEWS RELEASE WAS ISSUED SUGGESTING THAT THIS WAS A GOOD TIME FOR VOLUNTARY DISCLOSURES AND, WITHOUT PROMISING ANYTHING, NOTED THAT THE

LIKELIHOOD OF PROSECUTION WAS NOT HIGH IN THESE CASES. POLICY STATEMENT P-9-2, "PROSECUTION OF CRIMINAL INVESTIGATION CASES," INCLUDES VOLUNTARY DISCLOSURE AS A CRITERION IN DETERMINING WHETHER A CASE WARRANTS CRIMINAL PROSECUTION.

AMNESTY DOES OFFER THE POTENTIAL BENEFIT OF BRINGING NON-FILERS INTO THE SYSTEM, WHICH YOU MENTIONED. THERE ARE, HOWEVER, A NUMBER OF SERIOUS DRAWBACKS TO THE IDEA. FOR EXAMPLE, HONEST TAXPAYERS MAY PERCEIVE AN AMNESTY AS "SPECIAL TREATMENT" FOR DISHONEST TAXPAYERS, AND THEREFORE UNFAIR, INEQUITABLE, AND CONTRARY TO IRS' POLICY OF ADMINISTERING THE TAX LAWS UNIFORMLY. MOREOVER, INSTITUTING ONE AMNESTY MIGHT ENCOURAGE THE BELIEF THAT THE OFFER WOULD BE REPEATED IN THE FUTURE, LEADING TO NON-COMPLIANCE IN THE INTERIM. FINALLY, THE ADMINISTRATIVE DIFFICULTIES ENCOUNTERED EARLIER ARE LIKELY TO REAPPEAR, MAKING IMPLEMENTATION DIFFICULT.

WHILE WE ARE AWARE OF WHAT SEEMS TO BE AN INCREASING INTEREST IN THIS IDEA, AND ARE ALWAYS WILLING TO DISCUSS IT FURTHER, MY VIEW AT THIS POINT IS THAT THE IDEA DOES NOT WARRANT IMPLEMENTATION.

TAXPAYER SAFEGUARDS

YOU ALSO EXPRESSED AN INTEREST IN THE ADEQUACY OF THE TAXPAYER SAFEGUARD PROVISIONS IN TEFRA, AND WHETHER OR NOT THEY NEEDED IMPROVEMENT. AS YOU MAY RECALL, THE SERVICE PARTICIPATED IN THE EARLY DRAFTING OF THESE PROVISIONS, AND SUPPORTED THEM THROUGHOUT DEBATE ON THE BILL.

WE BELIEVE IT IS STILL TOO EARLY TO TELL WITH ANY CERTAINTY IF THESE PROVISIONS ARE WORKING AS INTENDED. ONCE WE HAVE MORE OPERATIONAL EXPERIENCE WITH TEFRA OVERALL, WE WILL BE IN A BETTER POSITION TO EXAMINE THE ADEQUACY OF THE SAFEGUARDS. YOU MAY BE ASSURED THAT WE WILL ADVISE THE CONGRESS IF WE FIND ADDITIONAL LEGISLATIVE MEASURES ARE NECESSARY.

WE HAVE PLACED EMPHASIS THROUGHOUT THE SERVICE ON THE NEED TO SAFEGUARD TAXPAYERS' RIGHTS, AND WILL CONTINUE TO DO SO; I TESTIFIED ON OUR EXTENSIVE SYSTEM OF SAFEGUARDS BEFORE CHAIRMAN RANGEL IN APRIL OF 1982. THE SUCCESS OF OUR VOLUNTARY SELF-ASSESSEMENT SYSTEM RESTS LARGELY ON TAXPAYERS' PERCEPTIONS THAT THE SERVICE IS FIRM BUT FAIR IN ITS ADMINISTRATION OF THE TAX LAWS, AND WE WILL MAKE EVERY EFFORT TO SEE THAT WE DESERVE THEIR CONFIDENCE.

Conclusion

Mr. Chairman, I have attempted to cover in my statement a few of the most significant efforts the IRS has made recently to simplify life for taxpayers. There are many other examples which I have not included here in the interests of brevity.

Some of our work began as efforts at internal efficiency and productivity, which also provided benefits to taxpayers; other advances were conceived and developed exclusively for the taxpayers' benefit. The common thread in both cases is the desire to do our job -- which by definition includes both internal efficiency and increases simplicity for taxpayers -- better. We are constantly striving to improve in both aspects of our job, in order to make the "service" in Internal Revenue Service more than just an empty word.

My associates and I will be pleased to answer any questions you or the Members may have.

Senator **Grassley**. Before I ask questions, I'll call on Senator Dole for his opening comments, and also, if you are under time pressure, to ask questions.

Senator **Dole**. No. I am just pleased to be here. We are pleased to have the Commissioner here, and others. I want to thank Senator Grassley for having these hearings. I think it is something we should do from time to time, and I may ask some questions after adjournment.

Senator **Grassley**. All right.

The short form 1040A is designed to be understood by a taxpayer with a 10th grade education—that's my understanding. And by that, we mean that the majority of the words on the form can be understood by an individual with a 10th grade education, rather than the concept embodied by the words.

Is the long form used by an increasing number of taxpayers? What is the reading level for understanding most of the words and phrases contained in the long form?

Commissioner **Egger**. In the 1040 form?

Senstor **Grassley**. Yes.

Commissioner **Egger**. I will call on Mr. Brooke to be more specific on that, but we are making every effort to work toward the 8th to 10th grade level of readability in as many of our publications and in as many of the instructions to all of the forms as we possibly can.

But Al Brooke, who heads up our effort in forms development, can be more specific on the readability. Al?

Senator **Grassley**. Mr. Brooke? Thank you.

Mr. **Brooke**. The current readability level of the 1040 instructions is now at the 11th grade level. Readability does not necessarily mean "understandability," since it is typically based upon a computer-base formula that computes the measure of readability based on the length of sentences, the length of paragraphs, and a number of technical words. Whenever possible we try to write the instructions to eliminate as many technical words as possible.

There are many words that seem to have only application in the area of tax law—those are difficult to deal with.

We also find that, as major legislation is enacted, for the first 2 to 3 years of that period before there is a general understanding of the impact of that type of legislation, that our readability levels tend to creep up a bit. We found that this year in the 1040A, which was at a lower readability before 1980, for instance, than it is now for the 1982 version.

Senator **Grassley**. Will you repeat your last statement? Your last sentence?

Mr. **Brooke**. The readability level of the 1040A has gone up slightly from 1980 through 1982, and we attribute that primarily to the fact that legislation has created signficant changes in the 1040A area, such as the charitable contribution deduction for nonitemizers, and the two wage-earner deduction. And in the early period of that type of legislation it is difficult for taxpayers to understand that because of the technical language, until we are able to further understand as time progresses, ourselves, how to better write those instructions.

Senator Grassley. My understanding is that only 50 percent of the population is able to read at the 10th grade level. Do you think that the inability of one-half of the population to understand the short form is having an adverse effect on compliance?

Commissioner Egger. I feel certain that the understandability, or readability, of our forms and publications is a factor in compliance, and that's why we are looking to simplification of forms for as many segments of the population as we possibly can.

With the 1040–EZ, for example, we estimate the universe to be something between 21 and 22 million out of our 95 and a half million filers, and that's a large segment of the population to be able to complete their filing obligation on this simplified form. And we are elated that as many as 15 million out of that universe did in fact use the form this year.

So in recognition of that problem, this is what we are trying to do.

The readability is one factor; but by designing the forms in sort of step-1-2-3 fashion, we can lead the taxpayers through the forms, even if some of the instructional material does require reading ability at the higher level.

Senator Grassley. How much time does your agency spend attempting to comply with the Paperwork Reduction Act?

Commissioner Egger. I doubt if I can answer that question at this point. I would have to accumulate that data.

Senator Grassley. You probably could submit it to us in writing?

Commissioner Egger. Yes; we would be glad to supply that, but it is substantial.

Senator Grassley. Would you be able to determine that without too much effort?

Commissioner Egger. Yes; we can provide a reliable estimate, because our counsel people and our forms people and a lot of others spend time on this.

Senator Grassley. All right.

[The information follows:]

Staff years expended to comply with Paperwork Reduction Act of 1980

Fiscal year:	
1981	32
1982	23
1983 (estimated)	25
Average annual staff years for fiscal years after 1983	23

The time spent by the Internal Revenue Service in complying with the Paperwork Reduction Act of 1980 represents the efforts of National Office and field personnel in analyzing forms and regulations containing reporting or recordkeeping requirements and in preparing clearance packages for OMB review. Also included is the time spent on special projects such as the Information Collection Budget and the identification and review of existing regulations containing paperwork requirements, as well as the time spent by Chief Counsel in interpreting and rendering opinions dealing with the Act. The Service's information reporting system does not routinely capture the time spent on paperwork reduction efforts. As a result, the above figures were developed on an ad hoc basis and are rough estimates.

Senator Grassley. Well, maybe the next question on this point is even more important. In regard to OMB's review of your efforts to comply with the Paperwork Reduction Act, what is OMB's turnaround time to you?

Commissioner **Egger**. I am going to make my own comments, and then again ask Mr. Brooke who spearheads that for us to comment.

We haven't had enough experience on the regulations. Only recently have we begun putting together the packages on regulations which OMB is now reviewing, and so we haven't got enough experience with that yet to really give you an idea; but on the forms, I would say that our experience has been pretty good.

Mr. **Brooke**. Yes; it has. OMB has 60 days under the act to review the form submissions that we send over, and typically we bunch them up. They have been complying with that portion of the statute; in fact, we have been able to get a very short turnaround time virtually whenever necessary.

Senator **Grassley**. Now, their review of the form is under the Paperwork Reduction Act? Or is that under another piece of legislation?

Mr. **Brooke**. No. It is under the Paperwork Reduction Act.

Senator **Grassley**. All right.

How much did the introduction of the 1040-EZ help you in reaching your paperwork reduction goals? Because it is my understanding that you have to reduce the number of lines on the tax forms to comply with the Paperwork Reduction Act.

Mr. **Brooke**. Yes; that's correct. The burden reduction generated from the approximate 15 million filers is about 7 million hours of preparation time. Within our information collection budget, that is approximately 1¼ percent.

Commissioner **Egger**. That is part of the problem, Mr. Chairman. The computation or calculation of the burden reduction leaves something to be desired, in my opinion, and as a consequence, even though we feel that the 1040-EZ was a major step forward in easing the burden on taxpayers, it doesn't reflect as all that significant in terms of the calculations.

Senator **Grassley**. I see.

Well, then, I am not trying to put words in your mouth, but would you be raising the point, implicitly, that the paperwork reduction act doesn't give you enough credit in meeting your agency's goal with such a major effort? Is there something about how we add up the score which causes this result?

Commissioner **Egger**. Yes; I think we and OMB agree that the calculation of the burdens and the amounts of it certainly need reviewing.

Senator **Grassley**. All right.

I am not sure to what extent I can be really precise in telling you about farmers' criticism of the so-called simplification of schedule F. We have had some complaints that this simplified form would be more difficult for them to complete.

I would just like to have your response. Do you understand what I am getting at?

Commissioner **Egger**. Yes.

Senator **Grassley**. You have heard the same thing I have?

Commissioner **Egger**. Yes.

The debate on the schedule F has gone on for a number of years. Those who are charged with the reduction in paperwork burden believe strongly that the reduction in the quantity of information on the schedule F is desirable from that standpoint; while our information from farm groups has been exactly the contrary, that they in fact like it. It provides an easy record for them to go from year to year in terms of keeping their records and formating them.

Al, you may want to comment some more on that.

Mr. BROOKE. Yes.

The current position of the Tax Forms Coordinating Committee, which is the function of the Service that is required to meet and make decisions on what will be on the forms, "is that schedule F basically isn't broken and it shouldn't be fixed." At this time our view is that schedule F should remain the same.

We are concerned about the detail of the income information that we do require, but we have talked to many, many people, including going to the Federal Register with different versions, and have found that generally the feeling is that it ought to be left alone. It has been relatively unchanged for many years; there is no strong basis for change.

Senator GRASSLEY. I guess I was getting the impression from the complaints that you are going through a process of simplification of schedule F. Then you are implying that you aren't going to change it right now?

Mr. BROOKE. We went through a process of seeking as much public input as we could on it, Mr. Chairman. We met yesterday on the form, and the view that we have based upon the respondents who have written in response to our Federal Register notice is that there is no overwhelming need at this time to change schedule F. Again, it is relied on significantly by the farmers.

Senator GRASSLEY. All right. And you are talking about the opinions of regulators, practitioners, and the taxpayers themselves?

Mr. BROOKE. That's correct.

Senator GRASSLEY. It's pretty unanimous?

Mr. BROOKE. It is not unanimous. No, Mr. Chairman.

Senator GRASSLEY. Well, no, but I mean overwhelming support for no simplification.

Mr. BROOKE. Yes. The views of most people, and particularly those they contact before they write to us, is that we ought not to change the schedule F. And then they have opinions on what we should do to it if we do change the schedule F.

Senator GRASSLEY. But you do hear from taxpayers on that, too?

Mr. BROOKE. Yes.

Senator DOLE. The question we receive the most real mail on—I would say "most mail without qualification except for the deluge of mail" on withholding——

[Laughter.]

Senator DOLE [continuing]. Concerns the taxpayer assistance programs. And as I understand, you indicated you are going to be at the same level in fiscal 1983. Does that indicate a change? Does the administration no longer seek to curtail or eliminate taxpayer assistance?

Commissioner EGGER. I will have to turn to the question a little bit differently, because I don't think that it is accurate, totally, to say that the administration wanted to curtail assistance. It was more a matter of trying to find different means of delivery of that assistance, because we weren't satisfied that the 800 or the toll-free telephone by itself was the sole answer.

I think perhaps it was an error for us to believe that we didn't need to keep that system to a degree, and we're moving toward changing that. But we are using, and we have used during the past filing season, a number of different techniques that we had not used in the past. One of them is Operation Outreach, in which we are sending people out to meet with taxpayers in small groups in public libraries and classrooms in evenings and on weekends—some in shopping centers.

We have used a new teletouch system this year in Newark. It is a video screen driven by a microcomputer, where taxpayers can simply develop for themselves answers to certain questions. We have had the same thing in telephones, so that some 400,000 people were calling in and listening to recorded messages this year on a long list of technical subjects and questions.

So what we are after is finding ways that we can more fully meet the needs of the public in terms of information, rather than just trying to cut back.

I think it is unfortunate that the proposed elimination of the toll-free telephone was viewed as just trying to cut off taxpayer information. It wasn't that at all; it was just that we were trying to go in different directions.

Senator DOLE. Has there been a significant increase in the taxpayers who itemize their deductions?

Commissioner EGGER. I'm sorry; I didn't hear that.

Senator DOLE. Has there been a big increase in the number of taxpayers who itemize their deductions?

Commissioner EGGER. Probably this year, but we won't know that until we have analyzed the information. We have perceived so far, based on our early statistics, that more people filed 1040 this year than in the past, and we suspect strongly that that is almost all in two areas—people now claiming child care credit and IRA deductions, which were not on the 1040A. As we have already said, we are planning to get those items on the 1040A for the next filing season so that then we will be able to tell more about it.

But I think the other factor may well have been interest rates, as more people incurred higher costs for home mortgage interest and things of that kind. It probably did increase slightly the number of people who would itemize as against those who would benefit as well from the standard.

[The information follows:]

TAXPAYERS ITEMIZING DEDUCTIONS

The Service does not yet have any firm data on the number of taxpayers who itemized deductions in the 1983 filing period. That information is developed through Statistics of Income (SOI) sources, and becomes available later in the year. However, preliminary indications are that itemized filings increased.

Treasury has estimated an increase of about 2.5 million itemizers for the 1983 filing period. This is in line with other recent increases of 2.7 million between 1981 and 1982 and 2.3 million between 1980 and 1981. (These increases were from 28.8 million to 31.5 million and 26.5 million to 28.8 million itemizers respectively.)

Senator DOLE. I guess if in fact it turns out to be a significant increase, it might mean we need to look at the zero bracket amount and whether or not we could raise that. If we could do it on a revenue-neutral basis, I assume you wouldn't object to that.

Commissioner EGGER. No, indeed. It simplifies our audit program considerably.

Senator DOLE. How much would we have to raise that to have any real impact? Have you given any thought to that?

Commissioner EGGER. I haven't, and I don't have any way of trying to respond to that. We could take a look at it.

Senator DOLE. That is something we might want to take a look at. I don't know where we would find the money, but——

On the issue of withholding, which we will be dealing with in our committee soon, it seems certain that there is going to be some change in withholding whether it is going to be repealed or whether it is going to be some compromise.

The President indicated in his press conference that he might be willing to accept a compromise. Whether or not he has the votes to sustain a veto is another matter; but it does seem to me we ought to try to preserve as much of the revenue as we can.

Frankly, I think withholding itself is good tax policy—I am not going to retreat from that—but when we don't have the votes, you have to retreat. One of the things we did in the Senate compromise was to seek—to improve the quality of information reporting.

Now, the IRS used to notify payors of interest and dividends when it determined that correct taxpayer identification numbers on such returns. Now, I understand that program was terminated or substantially cut back.

Commissioner EGGER. I don't believe we have terminated it. We probably have had to cut it back to some extent in recent years simply on a resource basis. But we have developed other techniques such as using computer searching techniques as a means of what we call tin perfection; that is, the perfection or correction of the taxpayer ID numbers on certain of the information returns. So we have been able to eliminate the necessity for that in part; but we have cut back, as I understand it, on the direct correspondence with some of the taxpayers.

Is that a fair statement, Jim?

Mr. OWENS. Yes, I think that's right. And second, the penalties that we have now in TEFRA, and hopefully the penalties we will have under whatever withholding system we end up with, will cause us to take another look at that and devote more resources to it. That way, hopefully, there will be a sufficient penalty there to encourage people to supply the correct number, or to supply the number if in fact it is not theirs.

Senator DOLE. It would seem to me, if in fact that can be done, it would still raise considerable revenue. You know, the big argument is, why isn't the IRS matching up all these 1099's? I was asked that question as recently as a half-hour ago in a speech.

Again, I don't know whether I want to go into withholding right here, but we were talking about taxpayers' burdens. By people not paying their taxes you are going to burden the rest of the people who are; so it's a burden on most people when we have to limit and we have to give up on withholding.

There is an answer to why you don't just match up all these 1099's and send them a notice, isn't there?

Commissioner EGGER. Yes, but I would like to just take a minute, because there is some confusion surrounding the whole question of our ability to match. I'd like to just take you through that, if I might.

We get about 450 million information returns in addition to the W-2's each year, and most of these come in—about 80 percent of them come in—on magnetic media. So the volume itself is not a particular problem.

The difficulty is that about 11 percent of those come in without a taxpayer ID number, or in some other unusable fashion.

Senator GRASSLEY. Can I interject at this point? You know, I kept using that statistic time after time after time with the Iowa bankers and savings and loans, and the credit union people, on this very debate. They sense that that's impossible, that it's not 100-percent numbers. Maybe they would agree with the fact there would be some that would not be correct; but they just—it's impossible for them to believe that we have 11 percent not there.

So I guess I am asking you—I believe that that's an accurate figure——

Commissioner EGGER. So do I.

Senator GRASSLEY. So I have been right in using it?

All right. I just want to tell you, though, at least in my State, what their reaction is when I use that 11-percent figure.

Commissioner EGGER. All right.

Now, keep in mind this is part of the reason why the TEFRA provisions are in there, in an effort to correct that, certainly to correct a significant part of it.

In addition to that kind of a processing problem, we also get a lot of aberrations. For example, we had one institution that sent us 200,000 1099's on magnetic tape, and then they sent us the same 200,000 on paper. And it so confused the system, we had to throw them all out. That kind of thing happens from time to time.

The other 20 percent that comes in in paper form, is simply a resource problem. We do not have enough people to key in 100 percent of the paper. So what we have been doing is sampling the paper—that is, putting in about a 15 to 20 percent sample of the paper documents, and 100 percent of the magnetic media items.

Now, we run these, then, against our master file information in order to develop the mismatches. When we do that, the mismatch is an aggregate number—total interest, total dividends, whatever. And then it is necessary to physically pull the return, under our present procedures, and make a comparison, in order to determine that the taxpayer hasn't misclassified the item, to make sure that the taxpayer hasn't reported on some other schedule—something of that sort.

After we have made that determination, then we prepare for the taxpayer what we call a CP-2000. It's a notice telling them that we have noted this discrepancy. And if they agree that "here's the recalculation of the tax," they can send us a check.

Now, we get about somewhere around two-thirds response back that is a conclusive response. Either the taxpayer explains it, or pays the tax.

In the case where they do not, then it becomes necessary for us to proceed and to go right down the full line of the assessment—

that is, the 90-day letter, and the whole thing. And it is in this followup that the difficulties occur, because without the resources to go all the way through that followup we don't, as a matter of policy, make the start after the initial notice if we don't have the resources to follow it all the way up.

In addition, after we have followed up and we have made the assessment, then it becomes a collection problem from time to time. And in very small dollar amounts the cost of pursuing it is sometimes so much that it makes no sense to follow it all the way out. So we take other options such as refund offset and things of that kind, rather than direct collection enforcement.

So we do in fact, with the exception of the paper documents, match up as much as we can. But in the case of those paper documents, it becomes a resource problem.

Now, what we are doing for the future—and this will take some time—is to begin to move in the direction of machine readability in documents other than those that come in on magnetic media. And when we reach that point and we have the equipment, and we will read it into the system, there is no reason that we can't match 100 percent.

So it becomes a question of administration—once you have matched, how much resource time do you put into the physical comparison, and then the followup.

That's the story of it.

Senator DOLE. Plus, I guess there are some few million that don't even file returns. Is that correct?

Commissioner EGGER. Well, I have given you only the filers. Now, we have some 6 million taxpayers on whom we receive a 1099 indicating that they had income from one of these sources, and where we do not have a return.

Our statistics show that, of the 6 million, something around a third of those do in fact owe a tax liability; whereas, about two-thirds did not have sufficient income to pay a tax, or the tax was more than covered by withholding, et cetera.

So it is the followup on that roughly one-third or, say, 2 million or 2½ million taxpayers that again is expensive, because we have to contact the taxpayer, try to receive a return, and so on.

Senator DOLE. That is something that we are going to be addressing in the next few days.

How many years are we looking at until you are going to have all this matching capability?

Commissioner EGGER. It is some guesswork on my part, but I believe it is going to be 2 to 3 years.

Senator DOLE. But, as you have indicated, even though you are matching, that's not the whole story. Then you have to collect it.

Commissioner EGGER. The rest of it is the willingness to spend the resources to pursue relatively small amounts.

Senator DOLE. The figure we have been using is that you audit now less than 2 percent of the returns, which I don't think is enough. But to do what you would collect through withholding, you would have to audit or otherwise contact about 20 percent of all taxpayers; is that correct?

Commissioner EGGER. I don't think it would be a matter of a full audit, but we certainly would be increasing our taxpayer contacts significantly.

Senator DOLE. How many more people would that take?

Commissioner EGGER. We haven't costed that out yet, Mr. Chairman, because to do it on a full basis—that is to say, pursuing every single dollar—it might take 30,000 to 40,000 additional employees. It obviously would be something that I don't think is desirable.

Senator DOLE. That could be the No. 2 jobs bill, then. Right?

Commissioner EGGER. I don't think anyone really thinks that that kind of intrusiveness would be desirable.

Senator DOLE. I hope not, but some of those who voted against withholding were indicating that is what we should do. But I hope we don't get into all of that. We would have some real reaction, then.

Yes?

Mr. OWENS. Let me just make one point on the 2 years that the Commissioner referenced—it is about 2 years until we could get the equipment installed and do the optical scanning and machine reading etc. Now, you've got to add to that additional time when we would get the documents and when they would be matched, and then where the follow-on would begin. So you are really not talking about within 2 years being out collecting revenues; it's more like 4 to 5 years before you would really be collecting revenues from this system that he is referring to.

Commissioner EGGER. You see, it is about 18 months from the close of the taxable year involved before we are ready to start processing and sending out the notices.

Senator DOLE. Now, you indicate that the absence of followup resources prevents mailing computer letters to more than—I think you said 2 or 3 million of the 20 million underreporters. Now, if we end up with some provision on backup withholding, would that be an efficient mechanism?

Commissioner EGGER. Backup withholding certainly has its merits. Until we see its precise form, of course, we won't know exactly how efficient it will be. On the other hand, it would certainly be my hope that there would be some flexibility in the system which would permit us at least an option as to which way to go; so that we wouldn't be obligated necessarily to go one particular way, even though that would be much more costly than, let's say, a followup with our just written notices.

Senator DOLE. Senator Grassley wanted me to ask a couple more questions, then we will go on to the next panel.

We may have some additional questions which we can submit to you in writing. Of course we are in almost—I won't say "daily contact," but we have frequent contacts with the IRS in our official capacity.

Senator Grassley asks, "Is it true that a regulation might be delayed within the IRS because only one employee is knowledgeable about the project?" Would it make more sense to assign two people to a reg project to make certain someone is familiar with the work to date, in case one employee leaves?

Commissioner EGGER. I think it is a rarity when only one employee knows anything about a particular subject. It is true that we assign in our L&R Division of Chief Counsel an attorney to take the lead in the drafting of that particular regulation, and it may well be that if it is not a major project that only one person will be working on it at a time. But I don't believe that the time that is lost as a result of something of that sort happening is significant. I think the problem is the volume, and the problem is almost always at the review levels as distinguished from the drafting levels.

So it's as we go up through the review chain. Keep in mind that every single regulation that we issue is subject to review by the Tax Legislative Counsel's Office at Treasury as well as by our own review levels in Internal Revenue.

Senator DOLE. A second question: Many taxpayers are opting to use the 1040-EZ because of its simplicity and failing to claim permissable deductions and credits. In other words, they use it, but they don't take their deductions in credit. Is that a widespread problem?

Commissioner EGGER. We really don't know that.

Senator DOLE. You don't know it yet, probably.

Commissioner EGGER. This is the first year that we have had the EZ, of course. But there will be two problems with the EZ—one is that people will use the form when they have other income sources that need to be reported; so there may be some underreporting problem there. And then the other one, of course, may well be that they will miss out on deductions. This will be a taxpayer education problem, I think.

Senator DOLE. Right.

Mr. BROOKE. We also supply about two full pages of instructions in the package that is mailed to the taxpayer. It is a combined 1040-EZ and 1040A package, and the two pages are designed to get the taxpayer to the right form.

I have received no correspondence in my office whatsoever indicating that someone has foregone an opportunity to claim a deduction or a credit simply because of the existence of the 1040-EZ.

Of course, you can't look at a 1040-EZ and make that determination. You can look at a 1040A and see if it could have been filed on a 1040-EZ and wasn't; but you can't do the reverse because of the level of information that is on the form.

Senator DOLE. You indicate in your statement that there is a substantial increase in the regulations backlog. Are we going to be able to get that down in fiscal 1983 or 1984?

Commissioner EGGER. We are working very hard on it. We, together with the Treasury, have put into effect a streamlined process; namely, by assigning regulation projects to different categories. And in the category 1, which are the simplest ones, those are on a fast track, and so we are able to dispose of a fairly large number of regulation projects in a much faster timeframe. We are making progress.

Senator DOLE. Is some of that delay because of the Treasury-level review?

Commissioner EGGER. Yes, there is some delay there, of course.

Senator DOLE. Can you dispense with that step? Or is that required?

Commissioner EGGER. Well, we are trying to bypass the in-depth level of review in the simpler regulations in Treasury, and there is where the time is really being saved. We are making real progress, I think, in the regulations process; it's just that there is a lot of it.

Senator DOLE. Do you get a lot of mail thanking you for the great work you are doing at the IRS?

Commissioner EGGER. Oh, I don't recall that I have had very much mail like that in recent years. It's been more the other way.

Senator DOLE. Not too many taxpayers?

Commissioner EGGER. Well, we hope that it will improve.

Senator DOLE. What do you do with a letter like that when you get it? Do you have a meeting, or frame it, or call in a psychiatrist? [Laughter.]

Commissioner EGGER. If I get one, I'm going to do that. Yes.

Senator DOLE. Another question: We enacted some legislation to eliminate commodity tax straddles. Again, you talk about taxpayers' burdens, they didn't have any burden at all there for a while. But now some have indicated there is a lot of harrassment. They assert that you have moved a special unit into Illinois to look at all the Chicago traders, and that they have been the victims of discrimination.

I'm not sure if you can address that question.

Commissioner EGGER. I would be unable to address it in any depth here, except to say that as far as a special unit is concerned, that is not accurate.

In our post of duty in Skokie, Ill., we do have a group of revenue agents who have attempted to specialize and learn something about the commodity trading business. It is a very complicated business, and in years gone by we simply haven't had anyone who was expert enough in the field to deal with many of the problems. So we have had to go that route.

But as far as having any task force, or anything of that sort, that's not the point. This is simply a way of providing specialized information.

Mr. OWENS. Let me just add one thing to that, Senator. In terms of specialists, it's no different than any other program. We have specialists in certain parts of the country who specialize in petroleum or in the oil industry, in the construction industry, in the pharmaceutical industry etc. It just depends on a particular geographical part of the country where that is needed. And we will be doing this in the commodity area.

Senator DOLE. Well, that's been called to our attention. Of course, we did make a substantial change in the law, and I guess there is some feeling that, even though we changed the law, that we were going back and try to apply prior law; whereas, some think they ought to maybe pay the rate that we enacted last year—I guess in 1981.

Commissioner EGGER. I have had a number of discussions with the Treasury on this subject, and I think it might be helpful to arrange an executive meeting so that we could brief you more fully without making improper disclosures.

Senator DOLE. All right.

Well, Senator Grassley has no further questions, and I have no further questions.

We appreciate very much your appearance this morning. We will be working, as I have indicated, not in all of these areas, but in many of them. We get a lot of letters from a lot of constituents, and as chairman of the committee a lot of letters from out of State. A lot of people are just confused.

Every administration talks about simplification, and they keep thinking it gets more difficult. Is there going to be a line added to the return now to report tax-exempt interest? That has been suggested as one way to smoke out people who don't pay any taxes, and that it might be necessary to do that in order to comply with the new Social Security Act.

Commissioner **Egger**. We haven't made any decision on it, but I know it is under consideration.

Mr. **Brooke**. Certainly we would do something with respect to the Social Security Act, in terms of the affected taxpayers on that side.

With regard to regular taxpayers who don't receive social security but who have tax-exempt interest, at this time we have not planned on putting on a special line. As usual, we are always troubled with the amount of space we have available on the 1040; it is very tight as it is, but it is something that we would certainly look at.

Senator **Dole**. I am not certain whether that would add to compliance, but at least you could find out who is getting all of the tax-free interest in the country and not paying any tax.

That's an area we want to get into in a later hearing: Can we get some more money out of the compliance side? Before we start taking away tax cuts and indexing, we ought to be looking at those who aren't paying what they owe.

I read that very good article in U.S. News. There are still about $87 to $100 billion out there that should be collected. That's as much as in the Senate budget resolution last night—$85 billion over 3 years in revenues. I know we can't get it all; but if you have some ideas on how we can get $1 billion or $5 billion, or $10 billion, we would certainly like to have that information. And we hope to have another hearing on that soon.

Commissioner **Egger**. Very well.

Senator **Dole**. Do you have some ideas, perhaps?

Commissioner **Egger**. Not immediately, but we would certainly be happy to work with you on that.

Senator **Dole**. And then there is another $296 billion in tax expenditures in that area. I assume that you have probably discovered a few rather large, well some would say "loopholes," and some would say "incentives," that we might want to address before we start taking away tax cuts from working people, and indexing, and changing ACRS.

It just seems to me that we have an obligation in this committee to look at compliance and loophole tightening before we go back and hit people over the head for higher marginal tax rates. So we will be looking at your help in that area, too.

Commissioner **Egger**. Very good. I will be happy to work with you.

Senator **Dole**. Thank you very much.

As I understand, the next panel of witnesses is Mr. Aidinoff, Louis Mirman, Dennis Carlin, and David J. Silverman.

I want to welcome you to the committee. We are pleased you are here.

We would hope that you might be able to include your written statement in the record and then summarize it orally. Please proceed in the order you were called.

STATEMENT OF M. BERNARD AIDINOFF, ESQ., CHAIRMAN, TAX SECTION, AMERICAN BAR ASSOCIATION

Mr. **AIDINOFF**. Senator Dole, I am M. Bernard Aidinoff of New York. I am the current chairman of the section of taxation of the American Bar Association.

For your information, the American Bar Association held an invitational conference on tax compliance which many of your staff members attended, and the ABA itself is going to be conducting a 3-year funded study on the causes of noncompliance.

I would like to just briefly address the various areas which are mentioned in the press release, from the point of view of a tax practitioner.

Senator **DOLE**. Right.

Mr. **AIDINOFF**. First, How much progress has the IRS made in reducing the complexity of tax forms and their instructions?

It is important to remember that the complexity of the tax forms and instructions reflect the complexity of the law itself. Almost every year for the last 14 years Congress has passed major tax legislation which has required the IRS to change its forms and instructions.

Each year millions of taxpayers have to digest these changes, using new forms and instructions. Unfortunately, the annual changes in the forms impress upon taxpayers the complexity and increasing uncertainty of our tax laws.

Given the complexity and the almost constant change in our tax law, I believe the Internal Revenue Service has done a creditable job in making the tax forms and instructions understandable to most taxpayers.

The Commissioner has already spoken about form 1040-EZ, which I would have applauded; but you have devoted more than enough time to 1040-EZ.

Obviously form simplification is something that is going to be a constant battleground between trying to make forms simpler and at the same time giving information as to what a taxpayer's liability is.

The second subject is: How well has the Paperwork Reduction Act served to stimulate reduced complexity?

Obviously, in an agency like the Internal Revenue Service, part of its job all the time is to simplify forms. I suspect that, were we concerned only with the Internal Revenue Service, the Paperwork Reduction Act would be a meaningless piece of legislation, and probably is viewed by most of us as just increasing the necessary paperwork in order to comply with that act. But this is an uninformed view by an outside practitioner.

Senator **DOLE**. It is probably accurate, though.

Mr. **AIDINOFF**. The third question which is included in the press release is, Should taxpayer assistance programs be maintained or modified?

There are at least two kinds of taxpayer assistance. The first is the tax account assistance which informs the taxpayer of his or her account status, and which basically gives information to the taxpayer with respect to records that the IRS has. Obviously this is a necessary part of administration. When that assistance breaks down, it causes increased taxpayer frustration, and I'm sure inevitably leads to some form of noncompliance.

The most important kind of taxpayer assistance involves technical return preparation. If there is anything I can emphasize at this point, it is the importance of having available face-to-face technical return preparation assistance.

Obviously it is important to have some sort of telephone service. On the other hand, waiting at the end of a telephone after a long holding period just increases frustration.

I would like to emphasize the importance of continuing taxpayer face-to-face assistance, because I think it sometimes relieves a taxpayer of frustration with the system. It has a pychological effect which in the long run promotes compliance.

Your fourth question is: Does the IRS provide timely and accurate advice to taxpayers? Can the rulings and regulations process be improved?

Obviously the system can be improved. It is primarily a question of resources. From my own experience, I can say that the current administration is doing the best job that it can with the resources that it has and the complexity that it has got to face.

But I might point out that, if we had a little more time in connection with the processing of legislation, if there were more time for technical comment by practitioners and professional organizations on statutory language, there might be need for less regulation. If we could slow up our legislative process in the tax area, there might be less need for quite as many regulations and rulings dealing essentially with problems of interpretation.

Your fifth question, Does the current regulations backlog create problems? Obviously, with complex legislation it creates problems. But I think the Service and the Treasury Department are doing a very creditable job.

Should you explore amnesty arrangements? I think we should not fool ourselves that, while the formal amnesty program was abandoned in 1952, I think most practitioners believe that there is an informal amnesty program.

Certainly the Internal Revenue Service and the Department of Justice cannot possibly prosecute the number of instances in which there is a nonfiling of returns. It's got to make choices, and I think most practitioners believe that a voluntary disclosure will materially reduce the possibility of criminal prosecution.

The whole area of amnesty requires exploration. And I think the more important issues with respect to amnesty are not just with respect to nonfiling; they are, for example, What would happen if we had an amnesty arrangement which would be applicable to dividend and interest income in prior years? In a sense, the filing of false returns which did not include the full amount of dividend and interest income?

None of us know the answer as to whether that type of amnesty program would increase compliance in the future or not. Questions like that require study and perhaps a substantial amount of research.

With respect to the TEFRA amendments, I think all I can say is that the TEFRA amendments that you referred to are really just going into place, and I don't think anybody has really had a chance to judge them.

I would obviously be glad to answer any questions.

[The prepared statement of Mr. Bernard Aidinoff follows:]

May 20, 1983

Statement of M. Bernard Aidinoff

Before the

Subcommittee on Oversight of the Internal Revenue
Service, Committee on Finance, United States Senate

With Respect to

Hearings on Efforts to Reduce Taxpayer Burdens

I am M. Bernard Aidinoff of New York, New York. I presently serve as Chairman of the Section of Taxation of the American Bar Association. Except as to certain specific matters which I will identify, I appear before you as an individual. I believe, however, that many of my fellow tax lawyers will be in agreement with the views that I express.

In announcing this hearing, Chairman Grassley mentioned the compliance provisions of the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") which, in part, attempted to reduce the burden on honest taxpayers by encouraging compliance with our nation's internal revenue laws by all taxpayers. Recently, the Section of Taxation of the American Bar Association sponsored an invitational conference on income tax compliance, which was attended by approximately 130 invitees. Participants included not only tax lawyers and law professors, but economists, criminologists, sociologists, historians, accountants, present and former government officials, foreign tax officials, and state and local tax officials. The purpose of the conference was to discuss the extent, nature and causes of noncompliance with our federal tax laws and to analyze ways in which conventional and new techniques might be used to reduce noncompliance. In addition, the American Bar Association has established a Commission on Taxpayer Compliance to develop and supervise a long-range research project on the nature, categories and causes of noncompliance with our federal tax laws to be conducted by the American Bar Foundation. I therefore welcome the opportunity to discuss with your Subcommittee ways in which we can strengthen and support our tax system and reduce the burden on taxpayers of compliance with our tax laws.

I will address, in order, each of the areas of concern which were mentioned in the press release announcing this hearing.

1. How much progress has the Internal Revenue Service made in reducing the complexity of tax forms and their instructions?

It is important to remember that the complexity of the tax forms and instructions reflect the complexity of the law itself. Almost every year for the last fourteen years Congress has passed major tax legislation which has required the Internal Revenue Service to change its forms and instructions. Each year millions of American taxpayers have had to digest these changes in using new forms and instructions to prepare their tax returns. Unfortunately, the annual changes in the forms and instructions impress upon taxpayers the complexity and increasing uncertainty of our tax laws.

Given the complexity and almost constant change in our tax laws, the Internal Revenue Service has done a creditable job in making the tax forms and instructions understandable to most taxpayers.

Each year during recent years the Internal Revenue Service has held public hearings on its forms and instructions and has invited public comments and suggestions as to how the forms might be improved and simplified. In addition, the Internal Revenue Service periodically meets with interested, knowledgeable groups (including representatives of the Section of Taxation) to discuss proposed changes in specific forms to improve and simplify them.

An excellent example of this Internal Revenue Service effort to reduce the complexity of tax forms is the 1983 payment voucher form for estimated taxes, Form

1040-ES. Millions of American taxpayers who pay their income taxes in four quarterly installments formerly had to fill in several blanks, sign and date, and return to Internal Revenue Service their quarterly voucher forms. Beginning in 1983, a taxpayer has only to fill in the amount of the quarterly payment and file the quarterly voucher form with the Internal Revenue Service. We also applaud the Internal Revenue Service's experiment with new Form 1040EZ which, provides a more simplified tax reporting form for taxpayers having less complicated financial profiles.

Although the Internal Revenue Service can, and undoubtedly will, take additional steps to reduce the complexity of the tax forms and instructions, meaningful reduction in the complexity of the forms and instructions will be accomplished only when our internal revenue laws themselves are simplified. Until then, despite ongoing efforts by the Internal Revenue Service to simplify the forms and instructions, they undoubtedly will continue to reflect the complexity of our tax laws.

2. How well has the Paperwork Reduction Act served to stimulate reduced complexity in the Internal Revenue Service forms?

Information concerning the impact of the

Federal Paperwork Reduction Act of 1981 on the tax forms has been so insubstantial that I am reluctant to express an opinion concerning that impact. My instinctive feeling is that there has been little impact other than an increase in paperwork to comply with this Act.

3. Should taxpayer assistance programs be maintained or modified?

There are at least two kinds of taxpayer assistance. The first is tax account assistance which informs the taxpayer of his or her "account" status - such as the whereabouts of a refund check, the status of an audit, or a claim for refund. This is an area in which only the Service has the answers and which entails a reporting based on records that the Service keeps. The Service has recently concentrated its efforts in this area, and I assume that it is continuing to upgrade this aspect of taxpayer assistance.

The second kind of assistance involves technical return preparation aid. It is important that the Service be given the necessary resources to continue this service.

Technical return preparation assistance is often the inducement that gets a low-income taxpayer "into the system." This assistance may be provided by volunteer groups or the Service. Without assistance, many taxpayers will simply not file. Since a good portion of these taxpayers are entitled to refunds (for example, from over-withholding) there is probably no immediate revenue loss, but the belief is formed in those people's minds that they do not have to file and continues during periods in which tax is due.

The preparation of a tax return is not a joyful occasion and is for many an intimidating experience. The fact that the answers to questions may be found in various Service publications or instructions is irrelevant. For those taxpayers (e) who are unable or unwilling to seek paid professional help and who cannot or will not understand the applicable tax law, the availability of a person with whom to sit down and go over the information for the return is a psychological necessity. The Service should provide a reasonable opportunity for taxpayers to receive this assistance and to perceive that the system operates in a fair manner. A recording at the end of a long telephone holding period that explains generalities of tax law is not adequate help or assurance.

The availability of face-to-face technical return preparation assistance by Service employees to taxpayers is an important aid in maintaining the integrity of the voluntary self-assessment tax system. Volunteer groups can and do help provide technical assistance and perhaps some day will provide a major portion of the needed aid. However, the availability of person-to-person Service assistance is needed today.

4. Does the Internal Revenue Service provide timely and accurate advice to taxpayers? Can the ruling and regulations process be improved?

In addition to the taxpayer assistance programs discussed above, the Internal Revenue Service provides advice to taxpayers in a number of ways including correspondence with taxpayers answering general questions concerning our tax laws; informal or letter rulings to specific taxpayers, which are based upon certain facts and which can be relied upon by such taxpayers in meeting their tax obligations; formal revenue rulings which are published by the Internal Revenue Service and the Treasury Department and which interpret the statutory provisions enacted by Congress for the general guidance of all taxpayers. Generally, the Internal Revenue Service has provided timely advice to taxpayers under all of these programs. However, because of the increasing complexity of our tax laws, these programs of the Internal Revenue Service are experiencing increasing strains, particularly in view of the budgetary and resource restrictions in recent years.

For example, because of personnel reductions, the Internal Revenue Service during the last several years has curtailed its letter rulings program by increasing the number of areas in which it will not rule. Each year during the last three years, the number of revenue rulings published by the Internal Revenue Service has declined from 367 in 1980 to 311 in 1981 to 228 in 1982. Each year during the last three years the number of final regulations (or Treasury Decisions) published by the Internal Revenue Service and the Treasury Department has declined from 77 in 1980 to 64 in 1981 to 55 in 1982. In addition, because of the uncertainty created by the continual changes in our tax laws and the reluctance of the Internal Revenue Service to issue letter rulings before regulations can be published, it is taking longer for taxpayers to receive definitive interpretations and rulings with respect to our tax laws. Finally, because of the frequency of changes in our tax laws, regulations have become substantially and increasingly backlogged during the last fifteen years. As the result of these problems, taxpayers and practitioners have had either to forego transactions involving tax uncertainties or proceed with the transactions without the benefit of Internal Revenue Service guidance.

It is important that Congress increase appropriations to provide the personnel and resources necessary to support and increase the Internal Revenue Service rulings and regulations programs. In addition, the Service should continue to adopt innovative approaches to improve its letter ruling, revenue ruling, and regulations programs. For example, I understand that the Internal Revenue Service is studying a change in its letter rulings program to decrease the length of time which it presently takes to receive and issue a ruling to a taxpayer. The change being studied apparently involves the use of a procedure similar to the "no-action letter" procedure presently being used by the Securities and Exchange Commission in which taxpayers and their representatives would describe a proposed transaction and the anticipated tax consequences, and the Internal Revenue Service would merely indicate whether it agrees or disagrees with the intended tax results. Such innovative changes should be encouraged.

To assist the Internal Revenue Service in identifying potential issues on which it would be helpful for the Service to publish revenue rulings, the Section of Taxation recently prepared and provided to the Internal Revenue Service approximately 100 topics or issues with respect to which the Service might issue revenue rulings for the guidance of taxpayers and practitioners. The Internal Revenue Service has responded enthusiastically and has published revenue rulings on many of the requested issues, and the Section of Taxation has adopted an ongoing project to provide the

Internal Revenue Service periodically with additional topics or issues on which revenue rulings might be published.

5. Does the current regulations backlog create problems for taxpayers? If so, how is that backlog to be reduced?

As previously indicated, until regulations are provided by the Service, letter rulings cannot be obtained.

Because of the speed with which legislation is written by Congress, there is an increasing tendency to leave difficult problems of interpretation to the Service and the Treasury Department. The result is often delay and confusion until the Service and the Treasury Department can provide meaningful guidance by issuing regulations and rulings.

There would be less concern about the regulations backlog if there were a greater opportunity and more time for technical review of statutory language and comment prior to the enactment of tax legislation. The timetable for tax legislation has been unduly compressed. Time should be allowed in the legislative process for review and input from interested, knowledgeable and constructive individuals and organizations to the tax-writing committees and staffs before legislation is enacted. For example, the members and staffs of the Congressional tax-writing committees and the Treasury Department have requested and been receptive to technical analyses and suggestions from the Section of Taxation in their consideration and drafting of tax legislation. Nevertheless, because of the press of legislative timetables, thorough analysis and review of proposed legislation is often not possible, and additional technical correction legislation has been required for virtually every major tax act during the last decade.

It is also important that appropriations to provide personnel and resources to support Internal Revenue Service activity be continued and enhanced. Approximately one year ago, my predecessor as Chairman of the Section of Taxation, in testimony before the Subcommittee on Treasury, Postal Service and General Government Appropriations of the Appropriations Committee of the House of Representatives testified in favor of increased appropriations for Internal Revenue Service compliance and taxpayer assistance programs. I wish to reemphasize my continued support for adequate funding of these Internal Revenue Service programs.

6. Should the Internal Revenue Service explore amnesty arrangements with nonfilers like those adopted by various states to bring such nontaxpayers into the tax system?

The question of whether the Internal Revenue Service should offer amnesty for those who have willfully failed to file federal income tax returns has a long and troubled history. Until January 10, 1952, the Internal Revenue Service had a general policy that if a taxpayer, before an investigation was begun, voluntarily disclosed to the Internal Revenue Service that he had willfully failed to file a return, the Internal Revenue Service would not recommend criminal prosecution. This policy was formally terminated in 1952. Since that time, neither the Internal Revenue Service nor the Department of Justice has had a formal amnesty policy. However, it is generally believed by most practitioners, based on substantial experience with the Internal Revenue Service, that the pre-1952 policy remains in effect today.

More important, however, is the need for Congressional and administrative attention to determine more about the causes of increasing willful noncompliance with our federal tax laws. Would an amnesty program with respect to the nonreporting of dividend and interest income and self employment income in past years promote compliance in the future? We do not know the answers. Additional investigation of the reasons for noncompliance is necessary. I urge the Congress and the Internal Revenue Service to devote additional resources and attention to this most important subject.

7. Are the taxpayer safeguard amendments of TEFRA adequate? If not, how may they be improved?

The taxpayer safeguard provisions contained in Sections 347-350 of TEFRA provide important protections to taxpayers with respect to the exercise by the Internal Revenue

Service of its power to impose liens and levies upon a taxpayer's property for the collection of taxes. Because these provisions are generally effective for liens and levies after 1982, we have had so little experience with them that I believe that any comments concerning their adequacy and need for their improvement would be premature.

Thank you for permitting me to testify today. I will be happy to answer any questions that the Subcommittee may have.

Senator GRASSLEY. Can we go through the whole panel before questions?

Mr. AIDINOFF. Sure.

Senator GRASSLEY. I need one clarification on what you mean when you talk about "slowing up the legislative process." Do you mean the problems that are created by our passing a major tax bill every year, or how we pass a tax bill?

Mr. AIDINOFF. How you pass a tax bill.

Senator GRASSLEY. All right.

Mr. AIDINOFF. I think your process is oftentimes too quick, and that as a result you have changes that are made in conference. There is really not time in the process to get professional and technical comments.

Senator GRASSLEY. The only reason I bring up the point is, I have received some criticism from constituents, and I'm sure other Senators have as well, that there used to be a period of time, maybe 2 or 3 years at least, before a tax bill would be passed, so that there was a settling and an opportunity to get used to one tax bill before you had to get used to another, and regulations could be kept more current.

Mr. AIDINOFF. Well, I do think that we have too much tax legislation, but sometimes it is just caused by the economy.

Senator GRASSLEY. Next in order would be Mr. Mirman.

STATEMENT OF LOUIS MIRMAN, PRESIDENT, NATIONAL SOCIETY OF PUBLIC ACCOUNTANTS, ALEXANDRIA, VA.

Mr. MIRMAN. My name is Louis Mirman, and I'm an accountant in public practice in Virginia Beach, Va. I am here representing the National Society of Public Accountants. I am presently the president of the National Society and a member of its executive committee.

Also, I am a past president of the Accountants' Society of Virginia, and I have been enrolled to practice before the Internal Revenue Service since 1959.

The National Society is an organization of over 17,000 professional practicing accountants located throughout the United States. It has affiliated State organizations in each of the 50 States, the District of Columbia, and the Commonwealth of Puerto Rico.

The members of the society are for the most part either sole practitioners or partners in moderately sized public accounting firms. The members provide accounting, auditing, tax preparation, tax planning, and management advisory services to individuals and to small and medium-sized business firms. Members of the society are pledged to a strict code of professional ethics and rules of professional conduct.

In response to the invitation to testify before this subcommittee regarding efforts to reduce taxpayer burdens, we submit the following observations for consideration:

We feel that the Tax Equity and Fiscal Responsibility Act of 1982, rather than providing important taxpayer protections, has created additional taxpayer burdens. Not only has it created additional reporting and compliance burdens but also continuing confusion in understanding the new tax laws, rules, and regulations.

We believe that the TEFRA tax penalty provisions designed to improve taxpayer compliance will instead fuel and encourage the increasing trend of deterioration of the tax compliance problem because of the complexity of the law. It seems that the Internal Revenue Service's attempt to clarify the Internal Revenue Code section 6661 penalty provisions confuses the issue.

Among the areas of concern regarding the IRS proposals under IRC section 6661 are proposed regulations section 1.6661-3 regarding the definition of substantial authority, the determination of whether substantial authority is present, and the types of the authority.

Most taxpayers do not own or have access to a sophisticated tax library, and even if they did could not begin to comprehend the provisions of section 6661.

In addition, it appears illogical under the IRS proposed rules that a taxpayer residing in a particular Federal judicial circuit does not have the judicial opinions of the courts considered in determining whether there is substantial authority for his position.

We believe the IRS has gone beyond the congressional intent, as indicated by the examples given in the committee report of what does not constitute substantial authority. In our opinion, the concept of substantial authority should be replaced by a reasonable-basis concept.

Another area of concern is the adequate disclosure rules contained in section 1.6661-4 of the proposed regulations. It appears unreasonable to expect the taxpayer to "red flag" his tax return for a virtually assured IRS audit in situations where there may be a legitimate controversial issue.

It is like a motorist driving at 56 miles per hour in a 55-mile zone, calling his speed to the policeman's attention by waving a red flag on top of the car. In the case of the taxpayer, the law requires him to call attention—that is, to make adequate disclosure—to items in his tax return about which there might be reasonable differences of opinion between the IRS and himself. Further, the taxpayer may view the tax preparer as representing the IRS rather than the client.

It seems that the provisions of the proposed regulations relating to IRC section 6661(b)(2)(B) (i) and (ii) are missing their target. The taxpayers that they aim to hit will be the very taxpayers who are making a very good faith effort to comply with the law. Those who comply will be penalized, while those who disregard the rules will escape the penalty.

An example of this type of situation is contained in the recently released report to the Joint Committee on Taxation by the Comptroller General: "IRS' Administration of Penalties Imposed on Tax Return Preparers," GAO/GGD-83-6, January 6, 1983, on page 28. According to some IRS district office and service center managers and examiners:

> IRS has been most successful in identifying and penalizing these preparers who have sought to comply with the requirements of the law. They base this belief on the view that IRS has been able to easily detect and penalize preparers who at least identify themselves on returns.
>
> Conversely, they believe that IRS has been less successful in detecting preparers who do not identify themselves on returns and/or commit conduct violations.

It seems that the penalty provisions of tax law and the proposed regulations are continuing a trend of the Congress and IRS to intimidate taxpayers with their overzealousness of penalty assessments. This, along with the complexity of tax laws, has worked to wreck tax compliance. There was a time when taxpayers were proud to support our country by paying their taxes; but now compliance is continually deteriorating under the burden of complex tax laws. Complexity is at the base of what is wrong with tax compliance.

Tax cheating has flared up over the past years because taxpayers perceive unfair treatment, particularly when they are trying desperately, in good faith, to comply, but they simply cannot understand what the tax laws are. To be unreasonably penalized by the law adds to their consternation.

Taxpayers need to be able to trust their Government; but at the moment they think that IRS is out to get them, and they consider this outrageous. IRS, therefore, should seek to improve its image, but it will not do so by promulgating regulations such as section 1.6661-3 and 1.6661-4.

Fair and effective administration of the Nation's tax laws is necessary if our voluntary self-assessment system of taxation is to survive. All of us has a duty to see that voluntary compliance does not deteriorate further. NSPA is concerned that the subjects we have discussed today tend to diminish voluntary compliance rather than to enhance it.

NSPA is pleased to have this opportunity to participate in these hearings on efforts to reduce taxpayer burdens. We shall be happy to work with this subcommittee and its staff in every appropriate way to achieve the goals of tax compliance to benefit all taxpayers and this Nation.

Thank you, sir.

[The prepared statement of Louis Mirman follows:]

STATEMENT OF
THE NATIONAL SOCIETY OF PUBLIC ACCOUNTANTS

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NSPA is pleased to have this opportunity to participate in these hearings on efforts to reduce taxpayer burdens. We shall be happy to work with this Subcommittee and its staff in every appropriate way to achieve the goals of tax compliance to benefit all taxpayers and the nation.

Senator GRASSLEY. Next is Mr. Carlin. And you may want to introduce, if you haven't already, the people who are with you.

STATEMENT OF DENNIS J. CARLIN, ESQ., CHAIRMAN OF THE FEDERAL TAXATION COMMITTEE OF THE CHICAGO BAR ASSOCIATION, ACCOMPANIED BY TED SINARS

Mr. CARLIN. I am Dennis Carlin. I am the chairman of the Federal Taxation Committee of the Chicago Bar Association. With me today is Ted Sinars, also on behalf of the Chicago Bar Association.

We are here to testify specifically on the amnesty for nonfilers program. We prefer to call it the remedial filing program—maybe that's a new term that can be coined. Currently most people have difficulty with the term "amnesty," as did our members of our bar association. That was one of the ways we were able to get it through.

As Senator Dole mentioned earlier, and as we can all tell from the budget hearings that are going on and from the possibility of the repeal of withholding tax, there is a need for revenue—new sources of revenue. And a likely source, in our view, is the underground economy.

Estimates of the Government are anywhere between $100 billion and $150 billion of unpaid taxes as the result of the underground economy. We are looking at a small part of that underground economy, the nonfilers, where the estimates are $5 billion in unreported tax.

If we can somehow garner this tax, it is an easy way to raise revenues, without, as Senator Dole said, "hitting the taxpayer over the head with higher rates." We must find a way to get these nonfilers on the tax rolls.

The Chicago Bar Association is recommending—as Ted will discuss in somewhat more detail—a voluntary compliance program. Admittedly this program is controversial. It has been discussed for a long time, and it was even controversial among the members of the Federal Taxation Committee of the Chicago Bar Association.

The program which we are recommending, which is a specific program, would grant immunity from criminal prosecution to nonfilers only. It really doesn't get into active tax evasion at all. The program, unlike other programs that have been discussed, uses objective standards, and the program terminates after a period of time; it is not a continuing program.

Our preliminary statement that was submitted this morning has a letter from the president of the Chicago Bar Association to the Senate Finance Committee, the House Ways and Means Committee, the Commissioner of Internal Revenue and the Chief Counsel, as well as the Attorney General. We have received responses so far from the Chief Counsel, and he has taken issue—and that letter is also a part of the statement—with our program. We plan to respond to him soon.

Interestingly, the Assistant Attorney General, Glen Archer, thought that it was a timely program and one that should be considered, and it was one of the first specific proposals that he saw.

As Mr. Aidinoff mentioned this morning, and I think even Commissioner Egger mentioned this this morning, the Government already has an informal disclosure program in existence. I guess we can call it an underground position. I think that it's time that the IRS go public with its position.

I would like to ask Ted to get briefly into some of the details of our program.

Mr. SINARS. Thank you.

Basically, our program provides that a delinquent taxpayer who files his returns before being contacted by the Internal Revenue Service or before the plan's termination date will not be prosecuted for failure to file tax returns. Correspondingly, we have an addendum to it which would allow a delinquent taxpayer who files a written notice with the Internal Revenue Service before being contacted by the IRS, that he intends to file his tax return which are delinquent and does so before the termination date, he also will not be prosecuted for failing to file his tax returns.

We agree with the Commissioner of the Internal Revenue, and our plan does provide that there is no waiver of the imposition of any of the civil tax ramifications. All civil taxes, penalties, and interest shall be and we encourage them to be collected by the Internal Revenue Service as any other taxpayer.

The plan is not open-ended; it has a defined termination date and is meant to be a one-time program, primarily until the IRS' computer system is brought up to date.

The plan has an objective standard, which can be understood by everyday taxpayers and not just lawyers. The plan is very similar to those which the IRS itself has adopted in the new TEFRA regulations. In the substantial underpayment penalty section of TEFRA, the regulations provide that if a taxpayer files an amended return correcting his initial return, or making a disclosure which was not on his initial return, automatically the penalty will not be imposed. This is precisely the same standard which we are tendering here with respect to failing to file. So if the Internal Revenue Service believes administratively they can handle it under TEFRA, we see no problem at all that they can't handle it here.

The plan applies only to misdemeanors of failing to file. It does not apply to the primary prosecution cases or tax evasion cases of the perhaps 1,500 criminal cases the IRS returns every year; only a minority are failure-to-file cases, and only a very small percentage of those cases, if any, will be adversely affected by this plan.

We recognize that the IRS cannot conceivably investigate, let alone prosecute, the millions of people who have failed to file their tax returns. And when we speak in terms of what Senator Dole said, "fairness," I think it is fair to all us taxpayers to have delinquent taxpayers pay their just share for the country.

We have touched base with numerous criminal tax investigators—special agents of the Internal Revenue Service—and, interestingly, they support this plan as well. These are the agents on the street, and they believe this plan should go through.

We believe the plan is meant for public announcement and not merely for the informal basis that practitioners are aware of, because most people who fail to file are not represented by tax practitioners; they are just unaware of what the IRS policy is.

We would encourage the IRS to consider this policy, and we thank you for allowing us to speak here today.

[The prepared statement of the Chicago Bar Association follows:]

Chicago Bar Association Preliminary Written Statement of Position on Delinquent Taxpayer Remedial Filing Program

THE CHICAGO BAR ASSOCIATION
29 South LaSalle Street
Chicago, Illinois 60603
Phone: 782-7348

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TREASURER

March 28, 1983

Mr. Kenneth W. Gideon
Chief Counsel
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Re: Remedial Filing Program

Dear Mr. Gideon:

As President of The Chicago Bar Association, I am writing concerning a matter we feel is important to the administration of federal tax laws. The Chicago Bar Association, at the instigation of its Federal Taxation Committee, herein formally recommends that the Internal Revenue Service adopt a remedial filing program in an effort to return numerous taxpayers to the tax rolls. As motivation for such action, we propose an objective standard which would protect the taxpayer from criminal misdemeanor prosecution for failing to file past due tax returns if the taxpayer complies with the directives of the proposed standard. This standard is as follows:

> A taypayer who has not filed income tax returns for one or more years shall not be charged with any criminal offenses relating to such failure to file if the taxpayer does file income tax returns for those years which the taxpayer believes are complete and accurate provided (1) that these returns are filed by June 30, 1984, and (2) that the taxpayer or a related entity has not been contacted by the Internal Revenue Service nor has received any correspondence from the Internal Revenue Service relating to any of the years for which the taxpayer has not filed. If a taxpayer notifies the Internal Revenue Service in writing of his intention to file delinquent tax returns and does file those returns prior to June 30, 1984, the taxpayer shall be entitled to the protections of the program with respect to those returns. Nothing contained herein will have any effect on the imposition of civil tax penalties or the collection of tax, penalties and interest.

The purpose of this plan is to assist the generable public by increasing the collection of taxes and to return numerous taxpayers to the tax rolls. We believe the Service can formulate this plan and present it to the public in a fashion to show the following positive aspects:

1. The Internal Revenue Service emphasis is on the collection of the revenue. The plan is meant to increase the number of taxpayers on the tax rolls and, correspondingly, increase revenue with proportionately minor administrative costs to the benefit of those taxpayers who are current in filing their returns.

2. Failing to file a tax return is a misdemeanor as opposed to filing a false return, which is a felony. Thus, the Service would not lose its primary prosecution cases.

3. In order to qualify for the plan, the taxpayer must file a return which he believes to be complete and accurate. If the returns are false, the taxpayer can be prosecuted for the felony of filing a false and fraudulent tax return. Thus, a taxpayer who elects this program stands in the same position as a taxpayer who has filed his return except that these delinquent returns filed under the program are more likely to be under audit scrutiny.

4. The remedial filing program applies only to criminal misdemeanor offenses and has no effect on the imposition of civil tax penalties or the collection of tax, penalties and interest.

5. The program has a defined termination date and is not open-ended. The proposed termination date of June 30, 1984 is flexible premised on the adoption date by the Internal Revenue Service. We recommend, however, that the program be available for a minimum of six months.

6. From an enforcement standpoint, after the plan's termination date, the Service may argue that a convicted taxpayer had the opportunity to clean the slate by filing delinquent tax returns in accordance with the remedial filing program but he willfully chose not to do so.

We believe this program can be successful since it applies an objective as opposed to a subjective standard to determine its application. A taxpayer must file delinquent returns or send written notice to the Internal Revenue Service prior to being contacted. Contact by the Internal Revenue Service means telephone, physical contact or correspondence with the taxpayer or a related entity, i.e., spouse, partnership or corporation in which the taxpayer has an interest. This objective emphasis is also understandable by the individual taxpayer as opposed to other suggested programs which promote interpretative nuances of attorneys. The plan is geared for national exposure through press releases, possible Internal Revenue Service assistance in the preparation of delinquent returns and perhaps even a cover letter with the form book mailed to taxpayers.

Prior to the submission of this plan to the Federal Taxation Committee and The Chicago Bar Association's Board of Managers, representatives conferred with our International Revenue Service Regional Counsel, Dennis Fox. Mr. Fox's commentary was of great assistance in defining the terms of the proposed standard.

Again, we request that the Internal Revenue Service review and adopt this standard in an effort to promote the fair administration of federal tax laws. We thank you for your cooperation and would appreciate hearing from you in this regard.

Sincerely,

David C. Hilliard

DAVID C. HILLIARD
President

DCH/ss
cc: Mr. Dennis Fox

bcc: Dennis J. Carlin
Burton H. Litwin
Theodore A. Sinars ✓

Copy of Chicago Bar Association Letter Sent To The Following:

Mr. Robert Lighthizer
Chief Counsel
Senate Finance Committee Professional
Staff
Room 2227 Dirksen Building
Washington, D.C. 20510

Mr. Robert J. Leonard
Chief Tax Counsel
House Ways and Means Committee
Professional Staff
Tax Staff
Room 1136 Longworth Building
Washington, D.C. 20515

Mr. Robert Dole
Chairman
Senate Finance Committee
2213 Dirksen
Washington, D.C. 20510

Mr. Dan Rostenkowski
Chairman
House Ways and Means Committee
2111 Rayburn
Washington, D.C. 20515

Mr. Roscoe L. Egger, Jr.
Commissioner
Internal Revenue Service
3000 IRS Building
Washington, D.C. 20224

Glenn L. Archer, Jr.
Assistant Attorney General
Tax Division
Department of Justice
Washington, D.C. 20530

Senator Charles Percy
Room SD 443
Dirksen Senate Office Building
Washington, D.C. 20510

Mr. John J. Salmon
Chief Counsel
House Ways and Means Committee
Room 1102 Longworth Building
Washington, D.C. 20515

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JOSEPH K. DOWLEY, ASSISTANT CHIEF COUNSEL
ROBERT J. LEONARD, CHIEF TAX COUNSEL
A. L. SINGLETON, MINORITY CHIEF OF STAFF

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, D.C. 20515

April 18, 1983

4 APR 1983
Chicago Bar Assn.

David C. Hilliard, President
The Chicago Bar Association
29 South LaSalle Street
Chicago, Illinois 60603

Dear Mr. Hilliard:

This is in reply to your letter to me, as well as to Rob Leonard and John Salmon of the Ways and Means Committee staff, concerning the Chicago Bar Association's proposal for a remedial filing program.

This concept has been discussed a number of times in recent years as a means of bringing non-filers back into the tax system, thereby improving tax compliance in this troublesome group. I am aware that the Internal Revenue Service has in the past had reservations about some aspects of such a program, but your proposal appears to adequately and reasonably address the concerns that come to mind.

I am forwarding your proposal to John E. Chapoton, Assistant Secretary for Tax Policy of the Department of the Treasury, and Roscoe L. Egger, Jr., Commissioner of the Internal Revenue Service, for their views. I will be in further contact with you once these responses are received.

Thank you for taking the time to share this with me.

Sincerely yours,

Dan Rostenkowski

Dan Rostenkowski
Chairman

DR:ppm

Copy sent to Messrs. Dennis J. Carlin, Burton H. Litwin & Theodore A. Sinars on April 27.

U.S. Department of Justice

Tax Division

Office of the Assistant Attorney General
GLA:mab

Washington, D.C. 20530

April 21, 1983

4 APR 1983
Chicago Bar Assn.

David C. Hilliard, Esquire
President
The Chicago Bar Association
29 South LaSalle Street
Chicago, Illinois 60603

Re: Remedial Filing Program

Dear Mr. Hilliard:

Thank you for your letter of March 31 urging that a remedial filing program be adopted in order to return delinquent taxpayers to the tax rolls.

Because of the growing concern and publicity about non-compliance with the tax laws, including the failure of some of the taxpaying populace to file tax returns, your suggestion to reconsider "voluntary disclosure," or "remedial filing programs," is quite timely. While some of us have from time to time given thought to restudying voluntary disclosure, your letter is the first specific proposal I have seen. We in the Tax Division will give attention to it. I have also taken the liberty of sending a copy of your letter, together with a copy of this letter, to the Chief Counsel of the Internal Revenue Service.

We appreciate the careful thought and consideration that has gone into your proposed remedial filing program and are grateful for the ideas which you, the Chicago Bar Association, and its Federal Tax Committee have put forward to improve taxpayer compliance.

Sincerely yours,

Glenn L. Archer, Jr.
Assistant Attorney General

cc: Honorable Kenneth W. Gideon
Chief Counsel
Internal Revenue Service
Washington, D.C. 20224

Copy sent to Messrs. Dennis J. Carlin, Burton H. Litwin and Theodore A. Sinars on April 27.

CHIEF COUNSEL
Internal Revenue Service
Washington, DC 20224

APR 26 1983

Chicago Bar Assn.

Mr. David C. Hilliard, Esq.
President, Chicago Bar Association
29 South LaSalle Street
Chicago, Illinois 60603

Dear Mr. Hilliard:

Re: Remedial Filing Program

I have received your letter of March 28, 1983 recommending that the Internal Revenue Service adopt a remedial filing program in an effort to return numerous taxpayers to the tax rolls. Your proposal resembles in some respects the Service's "voluntary disclosure" policy, which was abandoned in 1952. Under the voluntary disclosure policy, a taxpayer who made a truly voluntary disclosure of a willful violation of the Internal Revenue laws was not subject to criminal prosecution for that violation. This policy generated a substantial amount of litigation regarding what constituted a voluntary disclosure and the Service concluded that the problems created by the policy outweighed its benefits. Under current procedures, a voluntary disclosure of a tax violation by a proposed defendant is one factor which is considered in arriving at the determination of whether the case warrants a recommendation of criminal prosecution.

Your proposal attempts to use a more mechanical test, related to the timing of the disclosure, as a substitute for the concept of "voluntary". In my opinion problems similar to those encountered in the old voluntary disclosure policy would still remain unanswered. For example, the proposed standard applies to disclosures made prior to contact by the Internal Revenue Service with the taxpayer or other "related party" regarding a matter "relating to any of the years for which the taxpayer has not filed". In our opinion the meaning of the term "related party" and issues regarding whether the contact "related" to the years in issue would soon become the basis of heated litigation. Would contact by the Service with an employer, employee, customer, supplier,acquaintance or other witness who could reasonably be expected to provide evidence relating to the offense be a contact with a related party? Would the examination of a customer's or employer's tax liability, that will likely lead to discovery of the taxpayer's crime, be a related matter?

The proposal raises questions regarding the extent of disclosure necessary to qualify. Would the taxpayer be required to

Department of the Treasury

disclose his/her intent to defraud and any affirmative acts taken to defraud if evasion of taxes was intended? The fifty percent addition to tax for fraud may be dependent on full disclosure. Would denial of fraudulent intent when fraud could be proven allow the Government to prosecute?

Your letter says the proposal would apply only to misdemeanor prosecutions for failure to file; however, the proposed standard gives amnesty from prosecution for "any criminal offense relating to such failure to file". While a mere failure to file is a misdemeanor punishable under 26 U.S.C. § 7203, a failure to file combined with any affirmative act, the effect of which would be to mislead or conceal and thus defeat the tax, could give rise to a felony prosecution for willful evasion in violation of § 7201. If the proposal related only to a misdemeanor, a taxpayer who voluntarily disclosed that he/she did not file would not know at the time of disclosure whether there was still a possibility for a felony prosecution.

From the standpoint of tax administration, there is some doubt about the effect of your proposal upon voluntary compliance in the future. There is the possibility that some taxpayers who would otherwise timely file their returns may anticipate future amnesty programs and not file. There is also a possible negative reaction from those taxpayers who have filed timely returns and complied with the tax laws. Also unanswered is the affect such a program will have on prosecution of similarly situated taxpayers who were detected prior to the program.

The Service appreciates your interest and work in attempting to improve the tax system. This issue has been approached many times over the years and it has proven difficult to formulate a satisfactory answer. I have forwarded your letter to Mr. Donald Bergherm, the Associate Commissioner (Operations) for his further consideration.

Sincerely,

Kenneth W. Gideon

KENNETH W. GIDEON

Copy sent to Messrs. Dennis J. Carlin, Burton H. Litwin and Theodore A. Sinars on May 2nd.

Routing Slip

Internal Revenue Service

To	Symbol	Room	Action Code	Initial/ Date
[illegible]		3529		

- ☐ 1. Per our conversation
- ☐ 2. As requested
- ☐ 3. Approval
- ☐ 4. Comments
- ☐ 5. Information
- ☐ 6. Corrections
- ☐ 7. Signature
- ☐ 8. Initials
- ☐ 9. Note and return
- ☐ 10. Necessary action
- ☐ 11. See me
- ☐ 12. Call me
- ☐ 13. File
- ☐ 14. Prepare reply for signature of ________
- ☐ 15. Please answer by ________

Remarks

From	Phone	Room No.
	Date 4/22/83	

Form 1725 (Rev. 9-74)

U.S. Government Printing Office: [illegible]

THE CHICAGO BAR ASSOCIATION
29 South LaSalle Street
Chicago, Illinois 60603
Phone: 782-7348

OFFICERS
DAVID C. HILLIARD
PRESIDENT
THOMAS Z. HAYWARD, JR.
FIRST VICE PRESIDENT
JOHN D. HAYES
SECOND VICE PRESIDENT
JOSEPH L. STONE
SECRETARY
JOHN J. JIGANTI
TREASURER

March 31, 1983

COMMISSIONER
11374

Mr. Roscoe L. Egger, Jr.
Commissioner
Internal Revenue Service
3000 IRS Building
Washington, D.C. 20224

Re: Remedial Filing Program

Dear Mr. Egger:

As President of The Chicago Bar Association, I am writing concerning a matter we feel is important to the administration of federal tax laws. The Chicago Bar Association, at the instigation of its Federal Taxation Committee, herein formally recommends that the Internal Revenue Service adopt a remedial filing program in an effort to return numerous taxpayers to the tax rolls. As motivation for such action, we propose an objective standard which would protect the taxpayer from criminal misdemeanor prosecution for failing to file past due tax returns if the taxpayer complies with the directives of the proposed standard. This standard is as follows:

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2. Failing to file a tax return is a misdemeanor as opposed to filing a false return, which is a felony. Thus, the Service would not lose its primary prosecution cases.

3. In order to qualify for the plan, the taxpayer must file a return which he believes to be complete and accurate. If the returns are false, the taxpayer can be prosecuted for the felony of filing a false and fraudulent tax return. Thus, a taxpayer who elects this program stands in the same position as a taxpayer who has filed his return except that these delinquent returns filed under the program are more likely to be under audit scrutiny.

4. The remedial filing program applies only to criminal misdemeanor offenses and has no effect on the imposition of civil tax penalties or the collection of tax, penalties and interest.

5. The program has a defined termination date and is not open-ended. The proposed termination date of June 30, 1984 is flexible premised on the adoption date by the Internal Revenue Service. We recommend, however, that the program be available for a minimum of six months.

6. From an enforcement standpoint, after the plan's termination date, the Service may argue that a convicted taxpayer had the opportunity to clean the slate by filing delinquent tax returns in accordance with the remedial filing program but he willfully chose not to do so.

We believe this program can be successful since it applies an objective as opposed to a subjective standard to determine its application. A taxpayer must file delinquent returns or send written notice to the Internal Revenue Service prior to being contacted. Contact by the Internal Revenue Service means telephone, physical contact or correspondence with the taxpayer or a related entity, i.e., spouse, partnership or corporation in which the taxpayer has an interest. This objective emphasis is also understandable by the individual taxpayer as opposed to other suggested programs which promote interpretative nuances of attorneys. The plan is geared for national exposure through press releases, possible Internal Revenue Service assistance in the preparation of delinquent returns and perhaps even a cover letter with the form book mailed to taxpayers.

Prior to the submission of this plan to the Federal Taxation Committee and The Chicago Bar Association's Board of Managers, representatives conferred with our Internal Revenue Service Regional Counsel, Dennis Fox. Mr. Fox's commentary was of great assistance in defining the terms of the proposed standard.

Again, we request that the Internal Revenue Service review and adopt this standard in an effort to promote the fair administration of federal tax laws. We thank you for your cooperation and would appreciate hearing from you in this regard.

Sincerely,

David C Hilliard

DAVID C. HILLIARD
President

Senator **Grassley**. Thank you.

Mr. Silverman?

STATEMENT OF DAVID J. SILVERMAN, CHAIRMAN OF THE GOVERNMENT RELATIONS COMMITTEE OF THE NATIONAL ASSOCIATION OF ENROLLED AGENTS, NEW YORK, N.Y.

Mr. **Silverman**. Good morning. My name is David J. Silverman. I am chairman of the Government Relations Committee of the National Association of Enrolled Agents.

Our members are tax practitioners enrolled to represent taxpayers before the Internal Revenue Service. On behalf of our association I would like to thank the committee for the opportunity to speak this morning.

When the date of this hearing and the IRS hearing seeking recommendations from the public on ways to improve IRS tax forms was announced, our association contacted our membership throughout the country, requesting their recommendations. We were very pleased by the large number of responses we received.

On May 5 we submitted our report on ways to improve IRS tax forms to the Service. This morning I would like to submit our report entitled "Recommendations by the National Association of Enrolled Agents for Easing the Burdens of Taxpayer Compliance."

Mr. Chairman, I would like to speak briefly to the questions the Oversight Committee is addressing itself to.

With regard to reduction in the complexity of Internal Revenue Service forms, the Service has made great strides by simplifying the short form and by developing form 1040-EZ. These forms have been accepted by the public as a definite improvement.

The purpose of the short form—and for that matter, 1040-EZ—will be defeated if the code is constantly changed to allow taxpayers special deductions even if they don't itemize their deductions. By allowing deductions to taxpayers who don't itemize their deductions, the Service will end up with three types of long forms instead of the one now in use.

The National Association of Enrolled Agents wrote the President after his state of the Union address, requesting that he not propose any changes in the code until the sustained economic recovery is underway.

The simplest way to make tax forms easier is to stop what appears to be the annual revision of the code.

The membership of the National Association of Enrolled Agents recommends a moratorium through 1984 on any further changes in our tax laws—the only exception being technical corrections. Taxpayers need a breathing spell. Just when the public becomes experienced in using certain forms, the laws change.

The irony of some of these proposed changes in the code is that some of the changes don't have any effect on a taxpayer's ultimate liability, even when these deductions are claimed.

A case at point is the $25 charitable deduction that taxpayers may claim even if they don't itemize their deductions. Since the short form tax table increases at $50 increments, the Internal Revenue Service estimates that 50 percent of the taxpayers claiming this $25 deduction will still remain in the same $50 incremental bracket, and as a result the deduction will not have any effect on their ultimate tax liability.

The Paper Reduction Act has been monumental in reducing the number of forms that small pension plans were required to file with the Service and the Department of Labor. In this area the Paper Reduction Act has been extremely effective.

Our organization hasn't observed any major paper reduction in the basic forms the Service still requires to be filed in the area of income taxes. A lot is still to be accomplished in this area.

There has been a reduction in the amount of information required when it comes to filing employment tax forms. As I stated earlier, the Service annually holds hearings where it invites public comments on ways to simplify or streamline its forms. On May 5, 1983, such hearings were held in New York, Indiana, and Texas. The Service should be

commended for this type of program.

I believe the Internal Revenue Audit Manual should speak to the issue of the unnecessary documentation tax agents require during the course of a tax examination.

We realize that withholding on interest and dividends is a politically charged issue, but I can think of no other piece of legislation that could be designed whose effects would be to completely undo the progress made under the Paper Reduction Act. Congress, in reducing the flow of paper at one end, would be pumping in huge amounts at the other end by not repealing withholding on interest and dividends.

The taxpayer assistance program should be maintained, with one modification: It should be available on a 1 to 1 and group basis. We believe the Commissioner is correct in not wanting to provide individual telephone assistance. Many paid tax preparers take the easy way out and reach for the telephone when they have a question. The service should continue to implement its teletex information program.

With regard to the question: Does a taxpayer receive timely and accurate Internal Revenue Service advice? The answer is, not always. With the exception of the Problems Resolution Office, it currently takes 3 months or better to receive a reply to correspondence directed to a Service center. Many times the matter is in the hands of a collection officer before a reply is received.

Through my service as a member of the Commissioner's advisory group, I am personally aware of Commissioner Egger's dedication to the reduction of this response time.

Also, IRS field agents are routinely assigned to other areas or priorities in the middle of tax examinations. It is not unusual for agents to stretch out tax examinations for 1 or 1½ years because they were pulled off in the middle of an audit; and, accordingly, taxpayers find themselves in a state of limbo. Such delays necessitate the Service's need to obtain waivers of the statute of limitations—again, more paper.

In the past year our members have noticed that in some districts it can take 3 months or more to receive a final report from an agent after the examination has been concluded.

The last question that I would like to address deals with regard to the issue of nonfilers. We believe that the Service should restore the granting of amnesty to nonfilers whose assets or whose nonreported income is below certain levels.

In 1982 the Commissioner's advisory group recommended this to the Commissioner as a way of bringing nonfilers back into the system. Prior to 1952, the Service had a voluntary disclosure program, but pursuant to the information gathered by the Kind hearings before the subcommittee of the House Committee on Ways and Means that were held in January 1952, the Commissioner discontinued at that time this voluntary program of disclosure.

While I understand Commissioner Egger's reluctance to grant blanket amnesty, the Service should actively explore ways to bring the nonfiler back into the system.

It seems that the underground economy is the fastest growing segment of our economy.

Again, Mr. Chairman, I would like to thank the committee for the opportunity to make my views known this morning.

Thank you.

[The recommendations of the National Association of Enrolled Agents follows:]

RECOMMENDATIONS
BY
NATIONAL ASSOCIATION OF ENROLLED AGENTS
FOR EASING THE BURDEN
OF
TAXPAYER COMPLIANCE

1. Reduction In The Complexity Of Internal Revenue Service Forms

The Service has made great strides by simplifying the short form and by developing Form 1040EZ. These forms have been accepted by the public as a definite improvement.

The purpose of the Short Form, and for that matter 1040EZ, will be defeated if the code is constantly changed to allow taxpayers special deductions even if they don't itemize their deductions. By allowing deductions to taxpayers who don't itemize their deductions the Service will end up with three types of long forms, instead of the one now commonly used.

The National Association of Enrolled Agents wrote the President after his State of the Union Address, requesting that he not propose any further changes in the code until a sustained economic recovery is under way. The simplest way to make tax forms easy to use is to stop what appears to be the annual revision of the code. The membership of the National Association of Enrolled Agents recommends a moratorium through 1984 on any further changes in our tax laws, the only exception being technical corrections. Taxpayers need a breathing spell. Just when the public becomes experienced in using certain forms the laws change.

The irony of some changes or proposed changes in the code is that some of the changes don't have any tax effect on a taxpayer's ultimate tax liability even when these special deductions are claimed. A case at point is the $25 charitable deduction that taxpayers may claim even if they don't itemize their deductions. Since the short form tax table increases at $50 increments the Internal Revenue Service estimates that 50% of the taxpayers claiming this deduction will still remain in the same $50 incremental bracket and as result the deduction will not have any effect on their ultimate tax liability.

2. Paper Reduction Act

This act has been monumental in reducing the number of forms that small pension plans were required to file with the Service and the Department of Labor. In this area the Paper Reduction Act has been extremely effective.

Our organization hasn't observed any major paper reduction in the basic forms the Service still requires to be filed in the area of income taxes. A lot is still to be accomplished in this area. There has been a reduction in the amount of information required when it comes to filing employment tax forms. The Service annually holds hearings where it invites public comment on ways to simplify or streamline its forms. On May 5, 1983, such public hearings were held in New York, Indiana and Texas. The Service should be commended for this type of program.

The Internal Revenue Audit Manual should speak to the issue of the unnecessary documentation tax agents require during the course of a tax examination.

We realize that withholding on interest and dividends is a politically charged issue; but, I can think of no other piece of legislation that could be designed to completely undue the progress made under the Paper Reduction Act. Congress, in reducing the flow of paper at one end, would be pumping in huge amounts of paper at the other end by not repealing withholding on interest and dividends. The position of the National Association of Enrolled Agents is clear on this point.

3. Taxpayer Assistance Program

These programs should be maintained with one modification. It should only be available on a one to one and group basis. We believe that Commissioner Egger is correct in not wanting to provide individual telephone assistance. Many paid tax preparers take the easy way out and reach for the telephone when they have a question. The Service should continue to implement its Tele-Tax information program.

4. Timely & Accurate Internal Revenue Service Advice

With the exception of the Problems Resolution Office it currently takes three months or better to receive a reply to correspondence directed to a Service Center. Many times the matter is in the hands of a collection officer before a reply is received. Through my service as a member of the Commissioner's Advisory Group, I am personally aware of Commissioner Egger's dedication to the reduction of this response time.

Field agents are routinely assigned or reassigned to other areas in the middle of a tax examination. It is not unusual for agents to stretch out tax examinations for one or one and a half years because they were pulled off in the middle of an audit, and accordingly taxpayers find themselves in a state of limbo. Such delays necessitate the Service's need to obtain waivers of the statute of limitation. Again, more paper.

In the past year our members have noticed that it can take three months or more to receive a final report from an agent after the examination has been concluded.

5. Non-filers

We believe that the Internal Revenue Service should explore the granting of amnesty to non-filers whose assets or whose non-reported income is below certain levels. In 1982 the Commissioner's Advisory Group, recommended this to the Commissioner as a way of bringing non-filers back into the system. Prior to 1952, the Service had a voluntary disclosure program. Pursuant to the information gathered by the King Hearings before the Subcommittee of the House on Ways and Means that were held in January 1952, the Commissioner discontinued at that time its program of voluntary disclosure. While I understand Commissioner's Egger's reluctance to grant blanket amnesty, the Service should actively explore ways to bring the non-filer back into the system. It seems the underground economy is the fastest growing segment of our economy.

Thank you.

David J. Silverman
Committee Chairman

866 United Nations Plaza
New York, N.Y. 10017
(212) 752-6983

Senator GRASSLEY. Thank you.

I want to thank all of you.

The questions I have, except in one or two instances, are directed toward any or all of you on the panel who may want to respond.

I guess, first of all, I would like to start out by asking a question on the suggestion of whether or not a moratorium be placed on tax legislation. I guess from the standpoint of just raising taxes, it is likely our revenue needs will force us to examine the Tax Code. My philosophical approach is to agree with you; but from another standpoint, doesn't this recommendation ignore the extent to which aggressive and creative taxpayers are finding new and innovative means to avoid taxes?

Now, just recently we came across an example of a new type of corporate transaction invented just last November. It has been represented to save a single taxpayer $220 million over the next 5 years. Don't we need ongoing legislation to close loopholes as they are created?

Mr. SILVERMAN. I believe that is correct, but I was addressing myself mainly to granting specific credits, exemptions, and deductions to specific taxpayers in certain industries and in certain professions. I believe you are correct, Mr. Chairman, in wanting to have ongoing legislation to correct loopholes. I mentioned that when we suggested a moratorium, and the exception was technical corrections. And I think what you are proposing would fall under technical adjustments or corrections.

Senator GRASSLEY. All right.

Mr. Aidinoff?

Mr. AIDINOFF. Well, I certainly would not describe the particular instances as 'technical correction.' I might also point out that there were taxpayers who were taking advantage of that well before last November.

I think there is no question that you cannot put a moratorium on tax legislation. First of all, there are too many areas in which legislation is required becuase it has been promised for a long period of time. You don't have any choice but to work out your appropriate amendments to section 382.

On the other hand, there is a very strong feeling among practitioners that wholesale change in the law should be discouraged, that there should be an opportunity for legislation to have a chance to work, and to see how it works. There is a good deal of tax legislation which does not respond to the closing of loopholes but it just some very special legislation which on first reflection appears to be good, but after closer analysis may not be so good. And perhaps having a longer period between major items of tax legislation will in effect permit practitioners and the Congress to spend more time on items of tax legislation, perhaps, if we have major legislation say once every four years rather than every year.

Senator GRASSLEY. I don't think there would be too much basic philosphical disagreement between us.

Does anybody else want to comment?

Mr. CARLIN. Well, I would only add—I think Mr. Aidinoff mentioned it before—that some of the legislation that has been enacted recently is very difficult to implement and deal with for a practitioner, and part of the reason for this is that it has been enacted with such speed, where bar associations, or accounting associations or any taxpayer associations have not had an opportunity to give their views and assist in drafting some of this legislation.

I think the problems we are having as practitioners today is in really dealing with what exists now, and every time there is a new bill it makes it that much harder.

Mr. **Mirman**. The only comment I have, sir, is that quite often the legislation is passed retroactive, and then everybody has got a problem. And I wonder how much compliance is recognized then by the people who do not use practitioners?

I am sure there are a lot of people out there right now with small corporations that do their own work that haven't caught up with ACRS yet for 1981.

Senator **Grassley**. All right.

I would like to ask the representatives from the Chicago bar about the Illinois amnesty program and whether or not it could be applied on the Federal level, as you stated in your statement, or whether any modifications would be necessary.

Mr. **Sinars**. The Illinois program is already terminated. They had a defined termination date a couple of years ago, and the program, I understand, was very successful.

It is a very similar type program we are presenting here to the Federal system, where we would have a one-time defined termination date in an effort to collect a significant percentage of the $5 billion the IRS estimates is outstanding from failure to file.

Senator **Grassley**. So there wouldn't be any modifications in its application at the Federal level?

Mr. **Sinars**. There are no significant differences between the Illinois program as it applied to the Illinois Act and the program we are presenting here.

Senator **Grassley**. All right.

Mr. **Carlin**. Perhaps the only difference is adding a provision where, if a taxpayer gives notice and then files within the time period as opposed to having to go in to file his returns, this gives the taxpayer an opportunity to prepare setups. For example, a taxpayer has 5 or 6 back years' returns that he has not filed. It takes a long time to prepare these returns, and in the interim, while he is preparing the returns, he could be contacted by the Internal Revenue Service, and he would not be eligible for the program. If that taxpayer gives notice to the IRS first and in fact files within the period, then he would be covered as well.

Senator **Grassley**. I have a question. I didn't indicate to you in our announcement that we were interested in it, but it is something I have a personal interest in as I am also chairman of a subcommittee of Judiciary, working on equal access to justice.

So I would like to ask some or all of you: Is a taxpayer more likely to recover attorneys fees under the provisions of TEFRA or under equal access to justice? And do you see any problems in applying equal access to justice cases in the Tax Court? And, if so, what might those problems be?

Mr. **Silverman**. I would refer to the Bar on that.

Senator **Grassley**. All right.

Mr. **Aidinoff**. Well, I believe that the American Bar Association submitted testimony on this.

Senator **Grassley**. Yes, it did.

Mr. **Aidinoff**. Plus, I believe you got a separate statement, a supplemental statement, from the tax section.

I think the big concern is that we really shouldn't have two different rules.

Senator **Grassley**. You don't want to make a qualitative judgment about one over the other?

Mr. **Aidinoff**. Well, if you are not going to make a qualitative judgment in one area, I don't think you should make a qualitative judgment in the other. I think the two provisions ought to be the same.

I personally believe that TEFRA provisions are an appropriate attorneys fee provision, if we are going to award attorneys fees at all.

Senator **Grassley**. All right.

Well, we had the different standards for a year and a half, and I guess as you would view those different standards, how would you suggest which one might be the best, or whether or not you see any problems in applying the equal access to justice to the Tax Court?

Mr. **Aidinoff**. I think I would prefer to write you on that, Senator.

Senator **Grassley**. All right. I would appreciate that very much, and I would invite either or any and all of you to do that, if you would, please.

[The material referred to follows:]

125 BROAD STREET
NEW YORK, N. Y. 10004

FILE COPY June 1, 1983

The Honorable Charles E. Grassley,
United States Senate,
232 Russell Office Building,
Washington, D.C. 20510.

Re: Attorney Fees in Tax Cases

Dear Senator Grassley:

I am responding to a question you raised about attorney fees in tax cases during my testimony on May 20 before your Subcommittee on Oversight of the Internal Revenue Service. You asked whether I preferred the attorney fee reimbursement rules in the Equal Access to Justice Act ("EAJA") or those in the Tax Equity and Fiscal Responsibility Act ("TEFRA").

The American Bar Association and the Section of Taxation have long supported a provision for reimbursement of a prevailing taxpayer's litigation costs, including reasonable attorney fees. Neither the ABA nor the Section has taken any position on the relative merits of EAJA and TEFRA. The views expressed in this letter are therefore my own and not those of the ABA or the Tax Section.

The attorney fee rules in TEFRA were enacted in response to certain deficiencies in the EAJA as applied to tax cases, the most serious of which was that the EAJA was held inapplicable to tax litigation in the United States Tax Court. In addition to authorizing the Tax Court to award attorney fees, TEFRA responds to an unprecedented backlog of cases in the Tax Court by requiring taxpayers to exhaust their administrative remedies within the Internal Revenue Service to be eligible for attorney fee awards in court. TEFRA also specifically defines a "prevailing party" in tax cases to include a taxpayer who wins a significant issue of continuing precedential importance even though he may lose other issues which involve a greater amount of tax in the particular year in suit. Finally, TEFRA makes all prevailing taxpayers eligible for attorney fee awards, regardless of their net worth, subject to an overall limitation of $25,000.

The TEFRA rules could be improved. For example, many members of the tax bar believe that the burden of proof under TEFRA should be on the Government, as it is in the EAJA, since the Government is in a better position to explain why it brought or defended the case and why its position was reasonable.

Imperfect as they are, however, the TEFRA rules address the special problems of tax litigation while EAJA does not. Put to a choice, therefore, my recommendation is to stay with TEFRA. If Congress is dissatisfied with the way the TEFRA rules are working, changes should be made within the existing TEFRA framework.

Sincerely,

M. Bernard Aidinoff

Senator GRASSLEY. Now, one of the points that we have been concerned about here is the backlog of regulations. Because of that backlog I presume you find yourself having to request private letter rulings to a greater extent than if there wasn't a backlog, right?

Mr. AIDINOFF. No. One of the problems of the lack of regulations may be the inability to get a letter ruling. In other words, while a regulation project is going on, the Internal Revenue Service will in most instances not issue a ruling at all. And one of the problems with not having regulations out, particularly in final form, may be the inability to get a ruling at all.

Now, it is clear that if we have more regulations and the regulations are precise and don't avoid commenting on the difficult problems of interpretation, that there is less need for private letter rulings. And in that sense there is a very close interrelationship between the number of private letter rulings that will be requested, and regulations that are issued. But the lack of regulations really does not cause an increase in letter rulings; it just creates a vacuum.

Mr. SILVERMAN. Well, I believe the delay causes many taxpayers to interpret the code where they would like to see it interpreted. TEFRA, when it was enacted, had a provisions allowing H.R. 10 plans, the sole proprietors, to borrow funds. But a different section of the code, which was not repealed along with TEFRA, prohibited that. So many taxpayers find themselves looking at two conflicting sections of the code.

With regard to the backlog, I recall that when TEFRA was enacted granting taxpayers the right to invest in these all-savers certificates, and many banking institutions were coming up with rather esoteric financing arrangements for borrowing funds to let them invest in such things, the Service moved rather quickly to make it clear to the taxpayers and the investing public what they considered to be the correct interpretation of this law, and they did it in a matter of weeks, together with the Comptroller of the Currency. So I think the Service has demonstrated, on priority issues, they can move quickly and effectively in this area.

Senator GRASSLEY. Any other comments?

Mr. CARLIN. Well, just that I have been in the Chief Counsel's Office, working with L&R pretty actively. I think the problem they are having is that they just do not have enough experienced lawyers that are able to draft regulations at a fairly rapid pace.

I guess I always felt when I was there, it would be nice to have someone—it is difficult to have a new attorney out of law school cut his teeth on a set of regulations, especially on something as complicated as the Internal Revenue Code. I always felt that a 2-year field requirement or something before they enter into L&R would be good. I don't know if that's possible, however, because there just aren't enough people who are experienced enough that want to stay in L&R and draft regulations. I think that's the nub of the problem.

Senator GRASSLEY. All right.

On another matter, we have had the view expressed to us that because of form simplification the clientele aren't keeping as complete records as they used to. Do you see this as a problem among the people you have had to deal with? Or maybe I shouldn't limit it to the people you have had to deal with, but just generally?

And then, what recommendations might you have to improve the simplification effort, with or without that being a problem?

Mr. SILVERMAN. My experience is that so far it hasn't tempted people to discard records and not keep the records that are required.

I find that through the inflation of the past decade many wage earner taxpayers have now been escalated into rather significant tax brackets, and accordingly I think they are more aware of records and deductions that they might be entitled to. I think, then, I would agree with the Commissioner this morning when he recommended some safe harbor rules with regard to deducting travel and entertaining expenses—a per diem allowance instead of substantiation. I think, in my personal experience in my practice, more audits revolve around travel and entertainment issues. I think the Service's whole office audit program is centered on that. So some safe harbor rules could be promulgated to relieve taxpayers of the requirements of substantiation. I think that form simplification would be a great benefit to the Service and to the public.

Senator GRASSLEY. No other comments?

[No response.]

Senator GRASSLEY. All right. Those are all the questions I have. I want to thank each of you very much for your fine testimony, and particularly for your answers to our specific questions.

If it wasn't announced by Senator Dole, occasionally members who aren't here, or even, in the case of the Finance Committee, members on the full committee may write you questions to be answered in writing. We would appreciate that. And also the record will be held open for a considerable number of days. If you have anything additional you want to submit, I would appreciate it. Thank you very much.

[Additional material submitted for the record follows:]

NEW YORK STATE SOCIETY OF ENROLLED AGENTS
Government Relations Committee
SUITE 4050
866 UNITED NATIONS PLAZA
NEW YORK, NY 10017
(212) 752-6983

June 1, 1983

Senator Charles E. Grassley
Chairman
Senate Finance Oversight
 Subcommittee on the Internal
 Revenue Service
SR-246
Washington, D.C. 20510

Dear Senator Grassley:

I would like to thank you for being able to appear before your Subcommittee on May 20, 1983.

Congressman Leon E. Panetta of the sixteenth California district is sponsoring a bill, HR1540, which would allow Enrolled Agents and Certified Public Accountants to practice before the small case part of the United States Tax Court. Representative Panetta introduced this bill because he felt that taxpayers needed to be afforded additional relief when they had a tax dispute with the government.

Most taxpayers who obtain outside assistance in the preparation of the their tax returns employ Certified Public Accountants or Enrolled Agents who are authorized to practice before the Internal Revenue Service. However, if they get involved in a dispute with the Internal Revenue Service they must hire an attorney if they wish to take their case before the Tax Court. Our Association believes that enabling the taxpayer to make use of the individual who prepared his return would greatly expedite many cases before the Tax Court. The Commissioner of Internal Revenue and the Chief Counsel of Internal Revenue stated in their 1981 Annual Report that the number of small tax cases before the Court increased from 3,700 in 1977 to 10,500 in 1981. For your edification, I am enclosing page 75 of the 1981 report. In 1982, the Court received 9,800 small tax case petitions. Judge Tannewald only recently testified that the Court is straining under its current work load and is falling behind in its ability to dispose of docketed cases.

It is the hope of our Association that your committee will join in the sponsoring of legislation to afford the taxpayer with a small case tax dispute the opportunity for expeditious representation.

Very truly yours,

DAVID J. SILVERMAN
Committee Chairman

Tax Litigation

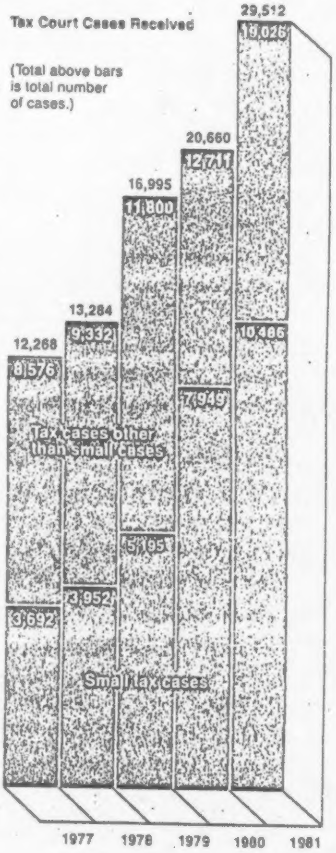
The Tax Litigation Division determines and coordinates the legal position of the IRS in order to assure consistency in all cases litigated in the United States Tax Court and all cases for refund of taxes and certain suits for declaratory judgment instituted by taxpayers in the United States district courts and the Court of Claims. If the IRS loses a case, the division determines, and advises the IRS with respect to Tax Court cases, whether to acquiesce or nonacquiesce in the decision and, with respect to other adversely decided cases, advises the Department of Justice whether or not to appeal.

During the 1981 fiscal year, a number of significant cases were decided.

- In *Rowan Companies, Inc. v. United States*, the Supreme Court ruled against the IRS, holding that Congress intended the definition of "wages" to be interpreted in the same manner for FICA and FUTA withholding as for income tax withholding, and, therefore, when meals and lodging provided by the employer are excluded from income tax withholding, they are also excluded from FICA and FUTA withholding.
- In *United States v. Darusmont*, the Supreme Court held that the application of an income tax statute to the entire calendar year in which the statute was enacted did not per se violate the Due Process Clause of the Fifth Amendment.
- The Supreme Court ruled for the IRS in *HCSC-Laundry v. United States*, holding that hospital-shared service organizations cannot qualify for exempt status under subsection 501(c)(3), but must qualify, if at all, under subsection 501(e) which governs cooperative hospital service organizations.
- The Supreme Court ruled for the Government in *Commissioner v. Portland Cement Co. of Utah*, holding that for purposes of computing gross income from mining by the proportionate profits method which, in turn, governs a taxpayer's depletion deduction, the first marketable product is finished cement, whether sold in bulk or bags, and that the costs of bags, bagging, storing, shipping, and selling should be included in the proportionate profits computation as nonmining costs.
- The Supreme Court ruled against the Government in *United States v. Swank*, holding that a provision in a coal mining lease permitting termination by either party on 30-days notice did not preclude the lessees from having an "economic interest" in the coal in place which would entitle them to a depletion allowance under sections 611 and 613.
- In *Diedrich v. Commissioner*, the Eighth Circuit ruled for the IRS, holding in direct conflict to previous net-gift holdings in the Fourth, Fifth, and Sixth Circuits, that a donor realized income on the gift of property to his children, who agreed to pay the donor's gift tax liability, to the extent of the excess of the donor's tax liability over his adjusted basis in the property transferred, an issue involving approximately 20 pending cases and between 4 and 5 million dollars.

Tax Court Cases Received

(Total above bars is total number of cases.)



Senator **Grassley**. Our next panel consists of David Keating, executive vice president of the National Taxpayers Union; Jack W. Wade, Jr., Arlington, Va.; Tom J. Donohue, president of Citizens Choice, and he is accompanied by John C. Lynch, their legislative counsel; and also Robert Capozzi, policy analyst of the National Taxpayers Legal Fund.

I would appreciate it if you would proceed in the way that I introduced you, please.

STATEMENT OF DAVID KEATING, EXECUTIVE VICE PRESIDENT, NATIONAL TAXPAYERS UNION, WASHINGTON, D.C.

Mr. **Keating**. Mr. Chairman, thank you for the opportunity to present testimony today on taxpayer compliance burdens.

My name is David Keating. I am executive vice president of the National Taxpayers Union. I commend the subcommittee for taking the initiative in holding hearings on this important issue.

The National Taxpayers Union has long been concerned with the burden from a tax code with excessively high tax rates, complexity, and uncertainty.

I would like to begin my statement by noting that income tax indexing, interestingly enough, is going to be important if we are to prevent the burdens of tax compliance from becoming heavier.

There are many other reasons, of course, for tax indexing; but one reason is simplicity and compliance. The zero bracket amount, or standard deduction, has been constant since 1979, yet the Consumer Price Index has risen substantially, and will continue to do so, no doubt. More taxpayers are finding it worthwhile to itemize deductions, resulting in more complexity in filing and complexity in recordkeeping.

I can answer Senator Dole's question: Yes, many more taxpayers are itemizing; 22.9 million taxpayers itemized in 1977, while 31.5 million itemized in 1981. That's an increase of almost 50 percent.

I would also like to point out that income tax indexing would prevent playing the audit lottery from becoming progressively more rewarding as taxpayers find themselves in higher tax brackets from the lack of indexing.

We would also like to recommend that Congress continue to explore ways toward massive income tax simplification. A simplified flat-rate income tax system would make most compliance burdens a thing of the past.

We believe that the taxpayer safeguard amendments in TEFRA were useful and an improvement over previous legislation, but we think they must be strengthened. I am sure that my colleagues on the panel will go into more detail on this; I would only like to bring up two particular points:

First, in TEFRA there is a provision for allowing award of attorneys fees, but there is a requirement that the taxpayer not only substantially prevail but prove the IRS was unreasonable. In our view, that is a very difficult burden of proof. At the very least, we think the burden should be on the IRS to prove that it was not being unreasonable. This is an important change that must be made if this provision is to be effective.

Second, we think it is also very important that the IRS should have to obtain a court order before seizing property. We think it is important that the IRS also exhaust all other methods of collection before seeking a court order. Every effort should be made to collect the tax in the least radical way. Should seizure be necessary, the independent judgment of a neutral party is essential to protect our citizens' basic rights.

I would like to also point out that section 701 of the Economic Recovery Tax Act of 1981 put a huge loophole in the Freedom of Information Act as it is applied to the Internal Revenue Service. No public hearings were held before this provision was placed into law, and as it is written it gives the IRS virtual carte blanche to not disclose data of any type. The data blackout will make it virtually impossible for independent researchers to monitor how fair or effective the IRS is in administering our tax laws. We believe the IRS is hardly the best judge of whether or not to disclose data which may reveal its own inefficiency or unfairness.

We have no quarrel with preventing disclosure of data that may prove harmful to tax collection, but that decision should be made by an independent party such as the courts, and not the IRS.

There is one other major point I would like to address, and that is, we believe the IRS has made substantial gains in simplifying the tax forms, but I am very disturbed about the 1040-EZ form. The 1040-EZ instructions say absolutely nothing about whether you should use form 1040A or form 1040. All the instructions say is whether you can or cannot use the form; there is nothing on whether or not you should use another form.

For example, there should be a sentence saying something like the following: "You may want to use form 1040 or form 1040A and pay less tax if you can itemize your deductions, claim adjustments to income, or claim tax credits you can't claim on form 1040-EZ."

I hope the subcommittee will request that the IRS do a followup survey of 1040-EZ filers to make sure that this is not a significant problem. We will never know unless someone does a thorough survey.

My time has expired, so I will conclude with two points. Another good idea that the IRS is starting to implement is creating safe harbors. The new safe harbor proposal on business meals is a very good idea, in our view. We would just like to make sure that these deductions are occasionally adjusted for inflation, at least more often than they currently are.

If there is anything we can do to help any members of the committee or the staff in helping to reduce taxpayers compliance burdens, we will be glad to help.

Thank you.

Senator GRASSLEY. Yes; and when the hearing is over, would you at some time in the near future contact Susan Hollywood of my staff to discuss the prospect of pursuing legislation.

Mr. KEATING. I certainly will.

Senator GRASSLEY. All right. Thank you. And Mr. Wade is the next one.

[Mr. Keating's prepared statement follows:]

Statement of David L. Keating

Executive Vice President

National Taxpayers Union

SUMMARY

Besides the burdens of high tax rates, the income tax system is too complex. The IRS has too many powers, and taxpayers too few rights.

Inflation has combined with the income tax code to make it more unfair while making it more complex. Taxpayers have found tax breaks increasingly important for their financial position.

To reduce tax compliance burdens, the following actions are essential:

- -- Income tax indexing must be preserved.
- -- Congress should take serious steps toward a simplified flat rate tax system.
- -- The taxpayer safeguard amendments of TEFRA must be strengthened and expanded. In particular, taxpayers should not have to prove the position of the IRS was unreasonable in order to qualify for fee awards before the Tax Court. Other key safeguards should include:
  - -- Requiring a court order to levy property, but only after the IRS has exhausted other methods of collection.
  - -- Requiring that installment agreements be binding.
  - -- Requiring a Miranda type warning to advise taxpayers of their rights before an audit interview.
- -- Tax form simplification should not result in taxpayers paying higher taxes. Form 1040EZ and the new Form 1040A do not do enough to alert taxpayers of deductions, adjustments to income, and tax credits for which they may be eligible.
- -- An amnesty program should be developed to bring non-filers and those taxpayers who have not reported certain types of incomes into the system. An amnesty program would benefit the IRS by bringing new taxpayers and more income into the system, while benefiting those taxpayers who need a fresh start without worry of criminal prosecution.

Mr. Chairman, and members of the Subcommittee, thank you for the opportunity to present testimony on taxpayer compliance burdens and legislative and administrative options to provide relief. I commend the Subcommittee for taking the initiative in holding hearings on these important issues.

The National Taxpayers Union has long been concerned about the heavy burden from a tax code with excessively high rates, complexity and uncertainty. In addition to these burdens, taxpayers must contend with the Internal Revenue Service (IRS), an agency which has extraordinary powers.

Our tax system is on thin ice. Recent public opinion surveys by the Advisory Commission on Intergovermental Relations show that the federal income tax is now perceived as the "worst tax - that is, the least fair." Tax protests by tax resisters are becoming more frequent and seem to be attracting a wider following. In the past, the problems of tax administration and tax compliance were easily papered over because tax rates for most taxpayers were not as high then. The past 20 years has changed this. Inflation has boosted taxpayers into ever-higher tax brackets, making deductions, tax credits and other tax loopholes increasingly important for taxpayer solvency.

Recent tax law changes have boosted penalties, interest, and reporting requirements, while doing little to protect taxpayers from unreasonable IRS actions or to provide for redress for unfair IRS actions. Information from the IRS, which was never easy to obtain, has been seriously slowed by recent legislation.

Tax Indexing Must Be Preserved

Income tax indexing must be preserved if we are to prevent the burdens of tax compliance from becoming heavier. There are excellent, and more important, reasons for preserving tax indexing on the basis of equity, government accountability, and economic efficiency. But income tax indexing is also important for simplicity and compliance. The "zero bracket amount" or standard deduction has been at $3,400 for joint returns and $2,300 for single returns since 1979. The Consumer Price Index is expected to rise over 45 percent between 1979 and 1984. More taxpayers are finding it worthwhile to itemize deductions, resulting in more complexity in filing and recordkeeping. 22.9 million taxpayers itemized deductions in 1977, while 31.5 million taxpayers itemized in 1981. Income tax indexing would prevent erosion in the value of the zero bracket amount and hold the numbers of taxpayers eligible to itemize relatively constant from year to year.

Income tax indexing prevents marginal tax rates from rising. As marginal tax rates rise, there is greater incentive to search for every additional dollar of deductions. Playing the audit "lottery" becomes more rewarding. Income tax indexing would prevent this situation from getting worse by keeping marginal tax rates stable.

Income tax indexing also removes an element of unfairness from the income tax system. Citizens rightly blame the federal government for causing inflation. The tax windfall that Congress reaps through the lack of income tax indexing is widely perceived to be unfair. Taxpayers in lower tax brackets commonly find that their income taxes rise at double the rate of inflation. It's the modern day version of taxation without representation.

Massive Tax Simplification Needed

Congress should continue to explore ways toward massive income tax simplification and adopt a flat rate tax such as S.557 by Senator Dennis DeConcini. The administrative burden of complying is caused by the complexity of the tax code. A simplified flat rate tax system would make almost all of these problems a thing of the past. The Finance Committee indicated last September that it would hold additional hearings on this issue. To date, these hearings have not yet been scheduled. We hope that they soon will be.

In announcing today's hearings, the Subcommittee indicated several areas of concern, including paperwork reduction and the current regulations backlog. Progress on these two problems is hampered by the steady stream of tax legislation that has been passed by Congress recently. A moratorium on new tax legislation would allow the IRS, not to mention taxpayers, to catch up with what Congress has wrought.

Taxpayer Safeguard Amendments Must Be Improved

The IRS's powers are unprecedented among government agencies, surpassing those of the FBI, the CIA and local police. Taxpayers' rights are few and far between. Even many of those rights can be ignored if the IRS decides that tax collection is in "jeopardy."

Americans are justifiably proud of our system of justice where people are presumed innocent until proven guilty. Unfortunately, when dealing with the IRS, the system is reversed.

Little imagination is needed to see that the IRS's powers represent a tremendous potential threat to our liberties. Numerous horror stories have surfaced documenting IRS abuses. Taxpayers have been personally harassed by

IRS agents in some cases. These abuses have been documented in previous hearings and in various news accounts and I will not discuss them here.

There remains little redress for taxpayers to battle unfairness. The IRS can simply assert a tax liability, knowing that it is often easier and cheaper for the taxpayer to pay than to battle unfounded IRS claims.

Last year, the National Taxpayers Union, Citizens Choice, the National Taxpayers Legal Fund, and other organizations closely worked together to identify some of the most common IRS abuses, and recommended a set of moderate, but important, reforms to be adopted by Congress. Although the National Taxpayers Union was not pleased with the overall content of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), we were pleased to see some of our recommendations incorporated in the taxpayers' safeguard amendments contained in TEFRA. Unfortunately, the most important one, award of attorneys' fees in tax litigation, was watered down to the point of being almost useless, while many of the more important reforms we recommended were not adopted.

The following provisions were adopted. First, the amount of property exempt from levy was raised, including the exemption for wages, salaries, and other income. Liens on property must now be released within 30 days once a tax liability has been satisfied or a bond has been accepted. The IRS must also, in normal situations, give notice in writing before making a levy on salary, wages or property. Property can now also be redeemed up to 180 days after sale, rather than 120 days. It also provides for compensation in case of wrongful levy.

Fee Awards: Taxpayers Should Not Have to Show The IRS Was Unreasonable

In the provision allowing for award of attorneys' fees, there's a requirement that the taxpayer not only substantially prevail but establish "that the position of the United States in the civil proceeding was unreasonable." This is a very difficult burden of proof. The government has the facts in its control as to why it pursued its action. At the very least, the burden should be on the IRS to prove that it was not unreasonable. This small, but important, change must be made if this provision is to be an effective taxpayer protection.

We have suggested in previous testimony that a formula approach to fee awards may be worth trying. The court now must decide whether or not the taxpayer "has substantially prevailed" in the "most significant issue or set of issues" or "has substantially prevailed with respect to the amount." It would be easier and more predictable to require that awards be based on the claim made by the IRS versus the assessment left once the case has been resolved by the Tax Court. For example, if there was a $10,000 claim by the IRS, but after litigation only a $1,000 assessment remained, the taxpayer could be said to have won 90 percent of the case, and would therefore be reimbursed for 90 percent of fees.

A Court Order Should Be Required to Levy Property

The IRS should have to obtain a court order to seize property. To obtain the order, the IRS should have to show by a preponderance of evidence that the taxpayer does indeed owe taxes to the United States. That taxpayer should also be given the right to contest the order before a court. Most important, a court order to levy property should be made only after the IRS has made a reasonable effort to enter into an installment agreement with the taxpayer and has exhausted all others methods for collection of the tax. Seizure of property is a serious step. Every effort should be made to collect the tax in the least radical way. Should seizure be necessary, the independent judgment of a court is essential to protect our citizens' basic rights.

Installment agreements agreed to by the taxpayer and the IRS should be binding, not only on the taxpayer but on the IRS. The only exception that should be permitted is where the taxpayer has clearly failed to provide adequate and accurate information concerning his financial position.

Written advice given to taxpayers by IRS employees should be binding. If the set of facts given by the taxpayer is correct, then advice rendered should be binding. When the IRS gives oral advice, the taxpayer should be informed that that advice is not binding on the IRS unless it has been put in writing. Taxpayers should be informed that oral advice cannot be guaranteed. This would not be difficult to do. It's not hard to imagine that a recording can be made for taxpayers who call the IRS telephone assistance lines. The recording could explain to the taxpayer that the oral advice is believed to be accurate but cannot be guaranteed. Alternatively, the IRS's information publications could give notice that oral advice can't be guaranteed.

Taxpayers should be allowed to have an audit at a place mutually convenient to the IRS and the taxpayer, provided it occurs within 60 days of the audit notice. Taxpayers should have the option of having the audit at the office of their attorney or other tax form preparer. Taxpayers should have the option of recording the interview. The IRS could also record the interview provided that the IRS informs the taxpayer of the recording and will make available the transcript if the taxpayer pays the cost of reproduction.

Audit Warnings Needed

The IRS should also give a warning in writing prior to the beginning of any interview stating that the taxpayer has a right to presence of an attorney or tax counselor familiar with the return. This statement should also include a Miranda-type warning that any statement made can be used against the taxpayer.

Although the taxpayer safeguard provisions in TEFRA did raise the amount of property exempt from levy, the amounts are still far too low. The exemption for personal property is a paltry $1,500 while the exemption for books or tools of a trade or profession is a mere $1,000. These limits should be raised to at least $10,000 and $6,750, respectively.

The current 30 day requirement for release of a lien is a fair and reasonable time. However, the ten day notice before property is levied is not enough. If the IRS needs 30 days to release a lien, certainly the taxpayer would also need at least 30 days to seek alternatives to prevent the levy from occuring. Ten days is just not enough time to arrange for the special financial changes that may be needed.

Freedom of Information

Section 701 of the Economic Recovery Tax Act of 1981 put a big loophole in the Freedom of Information Act as it applies to the Internal Revenue Service. It said "Nothing...in any...provision of law shall be construed to require the disclosure of...data used or to be used for determining [audit] standards, if the Secretary determines that such disclosure will seriously impair assessment, collection, or enforcement under the internal revenue laws." This provision was placed into law with no public hearings. As it is written, it gives the IRS a virtual carte blanche to refuse to disclose data of almost any type. A data blackout will make it virtually impossible for independent tax researchers to monitor how fair or effective the IRS is in administering our tax laws. The IRS is hardly the best judge of whether or not to disclose data that may reveal its inefficiencies or unfairness. Freedom of Information is a good principle which should apply to all federal agencies, including the IRS. We have no quarrel with preventing the disclosure of data that could harm tax collection. But the decision on what disclosures could be harmful should be made by the courts, not the IRS.

Tax Form Simplification

There is no question that tax forms need to be simplified. But simplification should not cause taxpayers to pay higher taxes. Unfortunately, Form 1040EZ is probably causing people to pay more tax than required.

The instructions for using Form 1040EZ say absolutely nothing about whether you should use Form 1040A or even Form 1040. All they say is whether you can or can not use this form. There should at least be a sentence in the instructions, preferably highlighted, saying "you may want to use Form 1040 or Form 1040A and pay less tax if you can: itemize your deductions; claim adjustments to income; claim tax credits you can't claim on Form 1040EZ."

Worse, on Form 1040A next to the box for single filing status are the words "see if you can use Form 1040EZ." This implies that single taxpayers should stop using Form 1040A and instead use Form 1040EZ if possible.

The new splashy and simplified graphics do make the short forms easier to work with. But they don't do enough to alert people to possible tax refunds or means of reducing their tax. For example, the old instructions for Form 1040A used to have a heading in bold, on page 2, titled "Who Should File a Tax Return." The paragraph that followed clearly said that even if you did not have to file a tax return "you should do so if Federal income tax was withheld from your pay, or if you can take the earned income credit. If either of these apply, you may be able to get money back from the government." The new instructions do not put this information in bold type. It is stuck at the bottom of page 3 in lighter type, has no headline and is only identified by the word "note." It is easily missed.

Other forms are slightly improved, but not significantly so. For example, Schedule A is better laid out this year than it has been in the past. Unfortunately, if you have a casualty or theft loss, you are required to file another form, Form 4864. In the past, you did not have to file a Form 4864 unless you had more than one casualty or theft loss.

Schedule SE, which has also been revised, is only slightly improved. Still, the obvious step toward simplification was not taken. The IRS should consider designing a form or worksheet for self-employed taxpayers who have no farm or partnership income.

Other worthwhile steps toward tax simplification are the creation of "safe harbors" for deductions. One example is the sales tax deduction for each state. Another example is the 20¢ per mile deduction for non-reimbursed automobile expenses. Also potentially helpful would be the proposed $14 deduction for business meals while away from home. But safe harbor deductions should realistically reflect a reasonable deduction and periodically be adjusted for inflation. Otherwise taxpayers will stop using them, causing additional complexity and compliance burdens for the taxpayer and the IRS.

Congress should eliminate penalties, under limited circumstances, for not paying estimated tax on time. Many retirees are penalized for not filing and paying estimated tax on time at the end of the first tax year during their retirement. Many of these people have been paying their income taxes on time for decades and some of them have never even heard of estimated taxes. Virtually all of them are willing to comply the next year but feel as if they have been unfairly treated for their mistake. I doubt that the IRS views this as being "reasonable cause" for abatement of penalty. A good solution would be to allow any taxpayer a one-time lifetime exemption for one tax year from penalty for non-timely payment of estimated tax.

Taxpayer Assistance Programs

Taxpayer assistance programs leave much to be desired. The thing that would gall most taxpayers most, if they knew, is the fact that there is a double standard in advice given. There's one quality of advice given to corporations and another given to individual taxpayers. Corporations can obtain rulings whose results are guaranteed. On the other hand, taxpayers who rely on oral or even normal written advice usually can't get a guarantee. In fact, some taxpayers have been slapped with negligence penalties for following oral IRS advice.

Amnesty Arrangements for Non-Filers

An amnesty program could benefit both the IRS and taxpayers. A properly designed amnesty program would benefit the IRS by bringing in untold billions of dollars from the underground economy into the light. The non-filer problem could be significantly reduced.

In the book When You Owe the IRS, author Jack Warren Wade, Jr. gives an example of a taxpayer who had not filed his returns for 11 years. Once the first filing deadine passed the taxpayer became too frightened to file in the following years. Even so, he would have been owed refunds for a total of $700 for the first six years. Then for the next three years, he owed money while in the last 2 years he was again due a refund, which in this case was large enough to pay all the back taxes. That year he came in and filed the return with Wade, who was then an IRS employee. The taxpayer "admitted that this problem had been bothering him for all 11 years. He had suffered two heart attacks, an ulcer, a nervous breakdown and countless sleepness nights worrying about what would ever happen if he got caught."

No doubt there are many taxpayers who would like to surface, but are scared about what the IRS might do to them. An amnesty program would allow taxpayers to voluntarily disclose past due taxes without worrying about criminal prosecution and jail. Various penalty and interest charges would still apply.

From the taxpayers' perspective there are several key provisions that should be considered as part of any amnesty program. First, the taxpayer must be certain that no criminal prosecution would result. This certainty may require legislation, particularly if the program lasts for more than a year. Otherwise, taxpayers may fear that the IRS could retroactively revoke the policy.

Second, there should be a requirement that the taxpayer not be contacted by the Internal Revenue Service concerning the tax return not filed or the income not reported in order to be eligible for amnesty. This is necessary to prevent the general public from thinking the program is insurance for those people who purposely evade taxes.

State and local authorities should be given time to implement similar programs. There is an exchange program between the IRS and state income tax collection agencies. An amnesty program would be far less effective if it became clear that taxpayers might be subject to criminal prosecution for not filing state and/or local income tax returns or not reporting some income on those returns.

A statute of limitations on owing tax should be considered. Some taxpayers may find it financially impossible to come forward voluntarily and pay their tax bills. There is currently a statute of limitations of six years on prosecution for failure to file a return but no limitation on owing tax. It may be worthwhile to also put a statute of limitations which limit tax liability to the six most recent years of liability, or net worth, whichever is larger. This would still enable the IRS to collect a large sum of monies owed, while not proving to be an impossible amount of tax to pay.

At the very least, the statute of limitations for obtaining a refund should be extended so that it parallels the statute of limitations on paying a tax. This would reduce the liability for those who came forward under an amnesty program as well as for future taxpayers who inadvertently let one filing deadline pass and then became afraid to file in the following years.

There is, evidently, a de facto voluntary disclosure policy which is known to sophisticated attorneys who specialize in tax fraud cases. But it's doubtful that the typical citizen is aware of such a policy. Instituting an amnesty program would end this double standard.

Mr. Chairman, I sincerely appreciate the opportunity to participate in these hearings. The National Taxpayers Union stands ready to assist you, the members of the Subcommittee, and the Subcommittee staff in reducing the burden of taxpayer compliance.

STATEMENT OF JACK W. WADE, JR., SELF-EMPLOYED TAX CONSULTANT, ARLINGTON, VA.

Mr. WADE. My name is Jack Warren Wade, Jr., and I am presently a self-employed tax consultant, and I am enrolled to practice before the Internal Revenue Service. I am the author of two very recent books on the IRS. My first book, "When You Owe the IRS," was released by McMillan Publishing Co. on April 15. My second book, "The Power to Tax; a Critical Look at IRS' Collection Powers," will be released shortly by the National Taxpayers Legal Fund.

My background includes 8 years with the IRS as a Revenue Officer, or tax collector. For 4 years I was employed at the Bailey's Crossroads Office of the Richmond District where I worked actual cases of delinquent taxpayers.

From September 1975 through September 1979 I was assigned to the National Office as a revenue officer, course developer, and instructor. For 3 of those years I was the program manager for the entire nationwide revenue officer training program. I wrote and produced 16 training publications for the Revenue Officer Basic Training Course.

First, Mr. Chairman, I would like to call upon the Government to declare a period of amnesty from criminal prosecution for the millions of nonfilers who would like to return to the tax system as dues-paying members of society. A properly administered amnesty program would help to restore people's faith in their Government, enhance the image of the IRS, and provide an opportunity for the Government to tackle the underground economy that, if left unchecked for another 10 years, could possibly destroy the voluntary compliance system as we know it.

The biggest benefit of an amnesty program is the increase of revenue that would immediately flow to the Treasury without the necessity to raise taxes. Based on IRS figures, I estimate that if only 20 percent of the nonfilers and underreporters avail themselves of the amnesty program, the Government could collect over $100 billion in the next 5 years.

Mr. Chairman, the amnesty program I propose will give delinquent taxpayers the once-in-a-lifetime incentives to right their wrongs and come back to the tax rolls before the IRS's increased staffing and computer capabilities make it ever more likely that they will be caught at enormous financial risks to themselves and the imposition of civil penalties.

My seven-point amnesty plan is outlined in the written statement.

My second proposal, Mr. Chairman, relates to safeguard provisions of the Internal Revenue Code, and more specifically to those provisions enacted under TEFRA. To the question, Are the taxpayers safeguard amendments of TEFRA adequate? I would have to issue a resounding, unequivocal No. The true fact is that there are almost no safeguards in the Internal Revenue Code to protect taxpayers against the arbitrary and capricious enforcement of the levy and seizure provisions of the code.

I can assure you, Mr. Chairman, that the Congress has just begun to provide safeguards for taxpayers, and that much more work needs to be done to identify gaps in taxpayers' rights, and to develop solid, concrete proposals for developing those rights.

In my new book "The Power to Tax" I have documented ways in which revenue officers violate IRS' own policies and procedures, and I have identified gaps in the code that allow instances of harrassment and abuse to occur.

I have also recommended at least 18 changes in the Tax Code that would give taxpayers some real protection against the misuse of IRS' awesome powers. All of my recommendations pertain to specific problems and abuses that I have identified in my book. A summary of those recommendations is included in the written statement.

For example, the TEFRA increases in levy exemptions were nominal and inconsequential, because the IRS had already recognized the same dollar exemptions by policy. Congress should take a real serious look at those exemptions and decide if the IRS should be allowed to seize and sell practically everything a taxpayer owns. I think the current bankruptcy laws probably give taxpayers more protection than the Internal Revenue Code.

Mr. Chairman, I have included a full summary of all my safeguard recommendations in my written statement. A complete discussion of each point, giving supporting reasons for changing the law, are outlined in my book "The Power to Tax" and have been reproduced for the written statement submitted by Bob Capozzi of the National Taxpayers Legal Fund.

I hope that my efforts have shed some light on the nature of the problems and what could be done to correct them.

I want to thank the subcommittee for inviting me to appear as a witness and giving me an opportunity to enter a statement into the record. As a former revenue officer, I am more than aware of the difficult and thankless job it is to collect delinquent taxes. I believe the recommendations I have made are reasonable and will go far to protect the rights of taxpayers without unduly restricting the ability of the IRS to perform its work efficiently.

I am available to the subcommittee at any time for additional consultation.

Thank you, Mr. Chairman.

Senator GRASSLEY. Thank you.

Mr. Donohue?

[Mr. Wade's prepared statement follows:]

WRITTEN STATEMENT OF

JACK WARREN WADE, JR.

Mr. Chairman:

It is my firm conviction that the voluntary compliance system, as we know it, is in great danger of collapse. The spiralling inflation of the '70s, and the budgetary cutbacks in IRS staffing and overhead during the same period combined to create an underground economy that has exploded to dangerous proportions. This "tax revolution" is chipping away at the foundation of respect that makes voluntary compliance work, and that makes our country the greatest in the world.

The trick now is to increase voluntary compliance and break the back of the underground economy without calling out the U.S. Army to back up the IRS, or turn the country into a police state. This is no easy task, and will require much work, dedication, creativity, and serious long-range planning with objectives that may even require an overhaul of the entire Tax Code. Since the problem of the underground economy is a complex one, there is no one panacea; but obviously, every small idea that tackles at least one aspect of the problem is a major step in the right direction.

In the past decade, many of our honest and hard-working citizens have tried to save money by either dropping off the tax rolls, underreporting their income, or exaggerating their deductions. The IRS estimates that in 1973 the losses to the government were around $29 billion. Today, the losses may be as high as $90 billion. Total losses over the past nine years may be as high as $500 billion, or one-half the national debt.

There is no need to explain or debate why this has occurred. What is important is that we bring these people back into the tax system as "dues-paying members" of our society, not only for the country's sake, but also for theirs. It is important to recognize that not all tax dodgers are criminals. Even Donald Regan has told Congress that the $90 billion tax gap is mostly caused by "honest people," who are otherwise law-abiding citizens who earn their livings respectably. Less than one-tenth of the tax gap is caused by illegal activities such as gambling, drugs, and prostitution.

My experience as a revenue officer has convinced me that many nonfilers are caught in a vicious web of delinquency they want to abandon but don't know how. Either unable to put their financial records in order, or to make sense of complicated tax laws, they go a year without filing and then don't file in subsequent years because of fear of being caught for nonfiling the previous year. Many of these people are truly afraid of the IRS and of going to jail. If they can be assured that they will not be prosecuted for coming forward, then a great contribution will have been made to restoring people's faith in their government.

A nonfiler never knows from one day to the next if he may be discovered by the IRS. Many are discovered as a result of IRS's resources. For example in F.Y. 1982, IRS secured or received over 1.3 million delinquent 1040s. But we also know that millions may never be discovered by the IRS and thus may escape paying any taxes at all. There could be as many as 12 million people who didn't file a 1040 last year even though they had a legal requirement to do so.

While some nonfilers aren't concerned or worried about this problem, many others are truly very scared and worried, and would like to be in compliance, but they have no way to right their wrong without fear of severe punishment. The prospect of criminal prosecution hangs like a veritable albatross during every filing season.

It is for these taxpayers that I am proposing that the government grant an AMNESTY from criminal prosecution to all tax dodgers, nonfilers and underreporters alike. A grant of amnesty would allow large numbers of these people to return to the tax rolls voluntarily and immediately. The government could be the recipient of billions of dollars in back and future taxes without even raising taxes. And, after all, collecting the revenue to fight a massive budget deficit is more important than maintaining compliance through the fear of criminal enforcement.

Practically, the government has very little to lose by enacting such a program and it would work because:

- there will be no cost or direct loss to the Treasury,
- the benefit of a guaranteed "no prosecution" pledge will appeal to many nonfilers and underreporters and will allow them to seize the opportunity while it is available,
- raising revenue without increasing taxes would be politically palatable,

- a temporary incentive to come forward would be the money saved from imposition of numerous civil penalties, which would otherwise apply if the delinquency is later discovered by the IRS, and
- the increased IRS staffing, new computer technology, new withholding requirements, and increased penalties will also encourage people to come forward once they realize what their future chances are of being caught.

I am proposing the following 7-point AMNESTY plan:

1. Whenever made effective, any person who has not already been notified by the IRS of the discovery of a nonfiling or underreporting may qualify for amnesty from criminal prosecution and from certain civil penalties for any past-due nonfiling or underreporting. The program would end within a defined time period: for example, six months may be sufficient.
2. Amnesty may be declared by writing AMNESTY across the top of a filed delinquent tax return or an amended return, or by filing an amnesty declaration with the IRS at the time of filing. Such declarations should be available at IRS offices and post offices, and would be signed upon request by various delegated IRS employees.
3. The IRS would waive all civil penalties, except the failure-to-pay penalty at 6%. Interest would be charged at the normal rate.

4. Persons declaring amnesty would be afforded liberal installment agreement privileges to pay their back taxes, as long as they comply with current withholding and estimated tax requirements; they would also be allowed to compromise their liability under appropriate circumstances.
5. The IRS must not be allowed to share any amnesty tax returns with any other government agency for the purpose of discovering nontax statute violations.
6. No person would be forced to reveal the source of his reported income if it would violate his rights against self-incrimination regarding any other laws.
7. Any return filed under the amnesty program that has been fraudulently prepared would be excepted from the amnesty provisions.

Mr. Chairman, if only 20% of the nonfilers and underreporters come forward, the government may increase its revenue by $100 billion over the next five years, a sum that would go a long way to assist in balancing the budget. Now is the time to take action before the underground economy destroys our voluntary compliance system.

SUMMARY OF RECOMMENDATIONS FOR A COMPREHENSIVE ACT TO FURTHER STRENGTHEN TAXPAYER SAFEGUARDS

The following is a summary list of recommendations being made by me to further strengthen taxpayer safeguards. The complete details of the changes being recommended and the supporting reasons for the changes are presented completely in my new book, "The Power To Tax - A Critical Look at IRS's Collection Powers." The full recommendations outlined in that book are reproduced in the written statement of the National Taxpayers Legal Fund presented today before this subcommittee.

1. IRC 6334(a)(2) and 6334(a)(3) which refer to exemptions from levy should be updated to recognize inflationary increases in taxpayers' property values.
2. IRC 6331(d)(3)(A) relating to the continuous effect of a levy on salary or wages should include provisions for a termination of the continuous effect when the taxpayer has entered into an installment agreement, or the IRS has determined that the taxpayer has substantiated a case of financial hardship.
3. IRC 6343(a) relating to Release of Levy should be amended to require the IRS to release a levy when the taxpayer either: enters into an installment arrangement, or substantiates financial hardship, or pays the IRS the U.S. interest in the seized property, or presents evidence that the value of the

U.S. interest is insufficient to meet the expenses of seizure and sale.

4. IRC 6331 should include a provision requiring the IRS to make written notification to the person whose property is being levied of the right of redemption under IRC 6337, and of the right of release under IRC 6343.
5. IRC 6331(c) relating to Successive Seizures should be amended to prevent a successive seizure within a 90 day period following a release of levy made either because the taxpayer paid the IRS the U.S. interest in the property, or because the value of the U.S. interest in the property was insufficient to meet the expenses of levy and sale.
6. IRC 6331 should include a provision requiring the IRS to issue regulations specifying the circumstances, conditions, and situations under which a levy will be made.
7. IRC 6334(a)(9), relating to minimum exemption from levy should be made applicable to the salaries and wages deposited in a financial institution.
8. The IRS should be specifically prohibited from making a levy when it is apparent prior to levy that the value of the U.S. interest in the property is insufficient to meet the expenses of seizure and sale.
9. The IRS should be prohibited from making a levy during the day a taxpayer is appearing at the IRS office to comply with a summons.

10. IRC 6331(a) relating to the 10 day notice and demand period should be amended to extend the notice and demand period to 30 days.
11. The IRS should be restricted from levying the following property unless it has been approved by the District Director or Assistant District Director:
    - (a) A principal residence of a taxpayer.
    - (b) An automobile used as primary transportation to and from work or employment.
    - (c) Tangible business property if the levy would result in the closure of the business.
12. The IRS should be required to issue a "Notice of Intent to Seize" within the 10 to 30 day period preceding the date of levy.
13. Taxpayers should be granted the right to file suit in a Federal District Court either prior to levy or subsequent to levy, to enjoin the IRS from selling the property, or to obtain a release of seized property when either:
    - (a) There has been an improper or illegal assessment.
    - (b) A deficiency assessment was made without knowledge of the taxpayer and without benefit of appeal.
    - (c) There has been a violation of the Tax Code, the policies or regulations of the IRS, or the Internal Revenue Manual.
    - (d) The IRS has made an unlawful determination that collection of the tax was in jeopardy.

(e) The value of the seized property is out of proportion to the amount of the liability, and other collection remedies are available.

(f) The value of the U.S. interest in the seized property is insufficient to meet the expenses of seizure and sale.

(g) The IRS will not release the seized property upon an offer of payment of the U.S. interest in the property.

(h) The IRS has arbitrarily established a minimum-bid price on the seized property in such a way as not to preserve or protect the taxpayer's equity in the seized property.

14. Taxpayers should be allowed to administratively appeal a decision to file a Notice of Federal Tax Lien when such filing would hamper or jeopardize collection of the tax.

15. The IRS should be required to issue a notice to taxpayers during any interview in connection with the assessment of a deficiency that the taxpayer has the right not to disclose any information or evidence that would violate his Fifth Amendment rights against self-incrimination.

16. The Ombudsman should be an appointee of the President who would serve a four-year term, and the Ombudsman should have the right to intervene in any enforcement proceeding when:

    (a) There has been an improper or possibly illegal assessment.

   (b) An assessment was made without the knowledge of the taxpayer and without benefit of the taxpayer's appeal rights.

   (c) There has been an action in violation of either the Internal Revenue Code, the policies or regulations of the IRS, or the Internal Revenue Manual.

17. Taxpayers should be granted the right for a judicial appeal of a levy made without regard to the 10 day notice and demand requirement as allowed under IRC 6331(a) when collection of the tax is in jeopardy.

18. Congress should legislate how the IRS is to establish the minimum bid computation prior to sale of seized property.

The National Taxpayers Legal Fund

Suite 116
201 Massachusetts Avenue, Northeast
Washington, D.C. 20002

(202) 546-5190

Excerpted from The Power to Tax by Jack W. Wade, Jr., published by the National Taxpayers Legal Fund. Submitted as written testimony to the Senate Finance Subcommittee on Oversight of the IRS by Robert Capozzi, policy analyst of the National Taxpayers Legal Fund, and Jack W. Wade, Jr., a former IRS Revenue Officer from 1971-79 and author of When You Owe the IRS.

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Recommendations For Comprehensive Legislative Reform

There is a greater probability of taxpayer abuse when IRS employees have more work than they can handle, more requirements than they know about, and unnecessary pressure to produce statistics. The problems of inefficient administration and potentially abusive actions will not disappear until those with decision-making authority, either in Congress or in the IRS, identify the problem areas and initiate reform. The success of the voluntary compliance system demands that the IRS "conduct itself so as to warrant the highest degree of public confidence in its integrity and efficiency." The following are recommendations for legislative reform which would expand the substantive rights of taxpayers and provide protection from IRS harassment and abuse.

RECOMMENDATION #1:

Congress should update IRC 6334, Property Exempt From Levy.

IRC 6334(a)(2) should be rewritten as follows: So much of the fuel, provisions, furniture, and personal effects of a taxpayer's household and of the arms for personal use, livestock, poultry, and other animals of the taxpayer's household as does not exceed $20,000 in value.

IRC 6334(a)(3)Books and Tools of a Trade, Business or Profession should be relabled and rewritten: Books, Tools, Machinery, Equipment, and other Property of a Trade, Business or Profession. So much of the books, tools, machinery, equipment and other property necessary for the trade, business or profession of a taxpayer, other than a corporation, as do not exceed in the aggregate $10,000 in value.

Reasons for Change:

Until the passage of the Tax Equity and Fiscal Responsibility Act of 1982, the exemptions of $500 for fuel, provisions, furniture and personal effects, and $250 for the books and tools of a trade, business or profession had not changed since the adoption of the 1954 code. Even though these exemptions were recently raised to $1,500 and $1,000, respectively, they still provide absolutely no protection for any taxpayers since they do not reflect the substantial increases in the cost of living since 1954.

The present law derives largely from an 1866 statute (Rev. Stat. 187) enacted primarily to collect excise taxes on cotton. Exemptions were allowed at $50 for fuel, $50 in provisions, and $300 in furniture, a total of

$400 which today is only exempted for $1,500. In 1866 the books, tools or implements of a trade or profession were exempted at $100; compare that to today's exemption of $1,000.

Section 6334(a)(2) presently only applies to a head of a household, meaning that such items are not exempted for single persons. In today's society where many taxpayers are single, and where increasing focus is placed upon the discriminatory aspects of our laws, the Congress should not allow this bias to continue.

The exemption allowed in IRC 6334(a)(2) should be raised to a level that would protect the average middle-class taxpayer's entire household effects. While the IRS has not made it a practice to enter into taxpayers' houses for the purpose of seizing property, the Supreme Court's *G.M. Leasing* decision now provides an opportunity for the IRS to obtain a court-ordered Writ of Entry to do so. Under the Writ procedure the IRS is granted powers equivalent to a search warrant. Rule 41 of the Federal Rules of Criminal Procedure (Title 18 U.S.C.) is the sole authority for the issuance, execution and return of federal search warrants, and does not authorize entry upon private premises to search for property to be seized for distraint purposes.

Now that the Supreme Court has ruled that such a search and seizure is permissible with the proper court-ordered Writ, the IRS now has the power to enter a taxpayer's residence and seize everything in the household but $1,500 worth of property, a paltry, insignificant sum. The IRS should not have the authority to seize and sell almost everything a taxpayer owns. The $20,000 limitation would be sufficient to protect almost every household in the country.

Section 6334(a)(3) should be changed to encompass other items that better reflect the essentials needed for an individual to be able to support himself. The right of an individual to be self-supporting needs to be recognized in the levy and seizure provisions of the Tax Code. The monetary amount is a better reflection of a minimum level of investment needed to be self-sufficient.

RECOMMENDATION #2:

Congress should rewrite IRC 6331(d)(3)(A) Effect of Levy to read: The effect of a levy on salary or wages payable to or received by a taxpayer shall be continuous from the date such levy is first made until the liability out of which such levy arose is either satisfied or has become unenforceable by reason of lapse of time, or the taxpayer and the Secretary have entered into an installment agreement, or the Secretary has determined that the tax is not currently collectible due to the financial hardship of the taxpayer.

Reasons for Change:

The Tax Reform Act of 1976 made two major changes in the Notice of Levy procedure. The taxpayer was granted a minimum exemption from the levy, as specified by IRC 6334(a)(9), and the levy became continuous until paid or the statute of limitations ran out. Previously the levy on wages, salaries, and other income was a "one-shot" affair — it took the entire net paycheck due the taxpayer at time of service, but the levy was released by payment of that amount.

IRS regulation 301.6343(a)(2)(V) provides for a release of levy when "the delinquent taxpayer makes satisfactory arrangements with the district director to pay the amount of the liability in installments." And as a practical matter, most Notices of Levy on wages, salary, and other income are released when the taxpayer comes into the office and an installment agreement is made. But the Internal Revenue Code makes no provision for the right of taxpayers to enter into an installment agreement, nor does it provide for the release of a levy for conditions other than full payment (IRC 6337), except when such release will "facilitate collection" of the tax (IRC 6343).

A collection manager might argue that a release of levy for an installment agreement would only "facilitate collection of the liability" when the amount to be paid under the installment agreement is greater than the amount to be received under the levy. From this kind of reasoning, the taxpayer has no protection.

A continuous levy could impose more of a hardship on taxpayers than the pre-1976 law which allowed the IRS to take the whole paycheck. But it was the intent of Congress to respond to situations where taxpayers and their families were left without funds to buy groceries. By codifying the provision to allow a release for an installment agreement, Congress will be assisting those taxpayers who would attempt to work out a way to pay their taxes, even though they were late in doing so. (Taxpayers typically get four notices before a levy is made and levies are usually made in nonresponse situations.) While the collection manual does specify that certain taxpayers "will be considered" for an installment agreement when they state an inability to pay the full amount for financial reasons (IRM 5231.1:(1)) and some taxpayers "will be granted an installment agreement for up to 12 months" automatically (those individual income taxpayers responding to notices; IRM 5231.3:(1)), there are large groups of taxpayers who do not fall under the automatic provisions, but who would enter into an installment agreement if the local IRS office would allow them to do so. Some collection managers do not like installment agreements and may refuse to release a levy when the taxpayer does not meet either the criteria for an automatic agreement or the manager's own peculiar policies.

A collection manager could decide that a taxpayer does not qualify under IRS's criteria for an automatic installment agreement because the amount received from levy is greater than the amount the taxpayer is proposing to pay each month under an agreement, and there are no other major assets for seizure. Since the law does not require a release of levy, and the taxpayer is not entitled to a release of levy per the Internal Revenue Manual, the levy will not be released.

The law also needs to be changed to provide for a release of levy when the taxpayer can demonstrate a "hardship." The IRS frequently suspends all collection action on a case when the tax cannot be collected because "it is determined that collection of the tax would prevent the taxpayer from meeting necessary living expenses." If the taxpayer comes into the local IRS office in response to a balance-due notice, the collection employee will obtain a Collection Information Statement, and if an inability to pay exists, the account will be suspended. But if the taxpayer does not respond to the notices, and IRS subsequently levies his wages or salary, then when the taxpayer comes into the office and presents a case of inability to pay, there is no Manual provision or Code section requiring the IRS to release the levy. Even though most collection employees would release the levy in a hardship case, the regulations pursuant to IRC 6343 do not provide for such a release. The taxpayer who presents his hardship case *after* the levy is served has less protection than the taxpayer who responded *before* the levy was served. The same inability to pay that existed prior to levy exists subsequent to the levy. A taxpayer's protection should not depend upon that kind of timing.

RECOMMENDATION #3:

Congress should rewrite IRC 6343(a) Release of Levy to read as follows:

> It shall be required for the Secretary, under regulations prescribed by the Secretary, to release the levy on all or part of the property or rights to property levied on where the Secretary determines: that such action will facilitate collection of the tax; or the taxpayer makes satisfactory arrangements to pay the tax in installments over a reasonable period of time; or the taxpayer can substantiate grounds for financial hardship; or the taxpayer pays an amount determined by the Secretary to be equal to the interest of the United States in the seized property, or the part of the seized property to be released; or where the value of the United States' interest is insufficient to meet the expenses of seizure and sale.

Reasons for Change

The regulations pursuant to IRC 6343 specify that the following conditions are considered to facilitate the collection of the liability:

Regulations (5382A) 301.6343-1.
Authority to Release Levy and Return Property

> Release of levy — **(1)Authority**.The district director may release the levy upon all or part of the property or rights to property levied upon as provided in subparagraphs (2) and (3) of this paragraph. A levy may be released under subparagraph (2) of this paragraph only

if the delinquent taxpayer complies with such of the conditions thereunder as the district director may require and if the district director determines that such action will facilitate the collection of the liability. A release pursuant to the subparagraph (3) of this paragraph is considered to facilitate the collection of the liability. The release under this section shall not operate to prevent any subsequent levy.

(2) Conditions for Release. The district director may release the levy as authorized under subparagraph (1) of this paragraph, if:

(i)Escrow arrangement. The delinquent taxpayer offers a satisfactory arrangement, which is accepted by the district director, for placing property in escrow to secure the payment of the liability (including the expenses of levy) which is the basis of the levy.

(ii)Bond. The delinquent taxpayer delivers an acceptable bond to the district director conditioned upon the payment of the liability (including the expenses of levy) which is the basis of the levy. Such bond shall be in the form provided in section 7101 and 301.7101-1.

(iii)Payment of amount of U.S. interest in the property. There is paid to the district director an amount determined by him to be equal to the interest of the United States in the seized property or the part of the seized property to be released.

(iv)Assignment of salaries and wages. The delinquent taxpayer executes an agreement directing his employer to pay the district director amounts deducted from the employee's wages on a regular, continuing, or periodic basis, in such manner and in such amount as is agreed upon with the district director, until the full amount of the liability is satisfied, and such agreement is accepted by the employer.

(v)Installment payment arrangement. The delinquent taxpayer makes satisfactory arrangements with the district director to pay the amount of the liability in installments.

(vi)Extension of statute of limitations. The delinquent taxpayer executes an agreement to extend the statute of limitations in accordance with section 6502(a)(2) and 301.6502-1.

(3) Release where value of interest of United States is insufficient to meet expenses of sale. The district director may release the levy as authorized under subparagraph (1) of this paragraph if he determines that the value of the interest of the United States in the seized property, or in the part of the seized property to be released, is insufficient to cover the expenses of the sale of such property.

There is additional criteria that the Collection Divison has imposed on IRC Section 6343 that is not stated in the regulations. Internal Revenue Manual section 5346.1:(1) reads:

> To facilitate collection of the liability, seized property may be released prior to sale for less than immediate full payment. As a condition to such a release, *subsequent full payment* must be provided for.

The imposition of the subsequent full payment rule makes sense if the taxpayer offers an escrow agreement, delivers an acceptable bond, enters into an installment arrangement, makes an assignment from his wages or salary, or agrees to extend the statute of limitations. The subsequent full payment rule does not make sense where it is imposed upon the release of a levy when the taxpayer pays the IRS the amount of U.S. interest in the property, or where the value of the U.S. interest is insufficient to meet the expenses of sale.

A taxpayer suffering the seizure of personal property should be able to have his property released to him when he can pay the IRS the same minimum amount for which the IRS would sell the property, or when the minimum amount for which the IRS would otherwise sell the property is insufficient to meet the expenses of sale. These releases should be a right of taxpayers even without the condition of subsequent full payment, or without regard for whether the release facilitates collection of the liability. Otherwise it is an abuse of taxpayers' property rights. The IRS should not be in the position of seizing and selling a taxpayer's property or property rights to an anonymous third party for less money than what it would cost the taxpayer to have his property returned to him.

This proposal would separate installment agreements, release where the value of U.S. interest is insufficient to meet expenses of sale, and release where the amount of U.S. interest in the property is paid to the IRS, from the pretext of "facilitating collection of the tax," and from the requirement that subsequent full payment must be provided for.

This proposal also codifies the main items listed in the regulations in order to give taxpayers rights that may be enforced in the federal courts, and which would not otherwise exist as regulations. As regulations, these conditions are not really "rights" of release. Instead, they are nothing more than procedural guidelines which, if not followed, cannot be enforced in court. In part, the conditions listed in regulation 301.6343-1 for release of levy are not mandatory. The regulation states: "The district director *may* release the levy..." It does not say the district director *will* release the levy. (The implications of this are further discussed in recommendation #4.) The IRS should be *required* to release levies in these situations.

The IRS would be required to establish regulations that would define a "satisfactory arrangement" and what is a "reasonable period of time." There are no regulations now existing on installment agreements. The only guidelines are contained in the Internal Revenue Manual, which are general enough to allow local managers to establish their own policies of implementation and their own interpretations of the regulations.

Taxpayers who communicate with the IRS prior to levy, and who are able to present a case of true financial hardship, are granted the privilege of not having to pay or being forced to pay their tax liability in full. IRS procedures allow collection action on hardship cases to be suspended until the taxpayer's ability to pay improves. Under the present law and regulations, which do not address the hardship case, a taxpayer who communicates with the IRS subsequent to a levy has no rights or benefits or privileges which were available immediately prior to levy. Even though most collection employees are compassionate enough to release a levy or Notice of Levy due to financial hardship, there is no specific Tax Code provision, regulation, or Manual directive that would allow or compel them to do so.

The fact is that a taxpayer experiencing a financial hardship *cannot* meet the provisions of regulation 301.6343-1 when combined with IRM 5346.1(1). It is therefore possible for the IRS to legally seize and sell almost everything a destitute unemployed taxpayer has (the exemptions from levy offer no protection either), simply because he may not be able to pay the full amount owed (per IRC 6337(a)), or enter into an installment agreement (by reason of his temporary unemployment), or even pay the IRS his forced sale equity in the property (per regulation 301.6343-1(a)(a)(iii) and IRM 5346.1:(1)). A law that provides no protection for these kinds of situations is a deliberate act of injustice.

RECOMMENDATION #4:

Congress should include a subsection within IRC 6331 to read as follows:

At the time any levy is made, the Secretary will make written notificiation to the person whose property is being levied of the right to redemption of such property under section 6337 and of the right to release of such property under section 6343 and the regulations pursuant thereof.

Reasons for Change:

Revenue officers and other collection employees are not required by any Code provision, any regulation, or any Manual directive to notify the taxpayer of IRC Section 6343, or even IRC Section 6337.

During a seizure, revenue officers will usually tell a taxpayer that the seizure will be redeemed (or released to the taxpayer) when *full payment* of the tax and all additions are paid, per IRC Section 6337. The IRM requires the revenue officer to demand full payment prior to seizure and by virtue of any direction to the contrary, compels revenue officers not to release the seized property for anything less than full payment. The Seizure and Sale Reference Guide (IRM Exhibit 5300-49 and IRS Form 4426) does not require the revenue officer to inform the taxpayer of the right to redeem per IRC 6337 or the opportunity of release per IRC Section 6343. It is possible, then, for taxpayers to assume that a seizure is a final act without any recourse, and that seized property is "lost property."

Revenue officers frequently play a game with taxpayers whose property is under seizure by demanding full payment for release and deliberately not informing them of the other release provisions for less than full payment. For example, a taxpayer owing $2,000 in tax and additions who has an automobile with forced sale equity of $500, may be told that $2,000 will bring about a release of the car, which otherwise may be sold to an anonymous third party for only $500. Usually the taxpayer is only informed of the other release provisions when it is evident to the revenue officer that he may have to sell the property. If the revenue officer has experienced a lot of problems with the taxpayer or has some type of vendetta or grudge against him, the revenue officer may not even inform the taxpayer of the release regulations and may let the property go to sale at forced sale equity in the absence of full payment.

The regulations pursuant to IRC 6343 state that the IRS "may release the levy" but *do not require* the release of the levy. This is more significant than a question of terminology. It means the IRS recognizes the redemption under IRC 6337 as a "right" of a taxpayer, but the release conditions as a "privilege." To emphasize this point, the section of Taxpayer and Third Party Rights (53(10)0), which spells out the "rights" a taxpayer has relative to levies, follows. Notice that the right of release of seized property per conditions specified in the regulations pursuant to IRC 6343 is absent. Only the "right to redeem" is listed.

Taxpayer and Third Party Rights

GENERAL

Service employees have the dual responsibility of protecting the interests of the Service while at the same time guarding the rights of taxpayers and third parties. Although the procedures in Chapter 5300 contain the information required to fulfill the responsibility, this section is designed to highlight the rights of taxpayers and third parties as they pertain to specific levy and sale actions.

RIGHT TO APPEAL

(1) Taxpayers who reach an impass when dealing with a collection employee have the right to have their case reviewed by a supervisory official. The name and location of the immediate supervisor should always be provided in such circumstances.

(2) In addition to supervisory review within the collection function, the taxpayer should be advised of the availability of the district Problem Resolution Officer.

(3) When an impasse occurs, the taxpayer should be advised of the appeal availability even though a higher level review is not requested.

DETERMINATION OF PROPERTY EXEMPT FROM LEVY

(1) Certain property of taxpayers is partially exempted from levy by Section 6334(a) of the Internal Revenue Code. When collection em-

ployees levy on those items subject to exclusions, they are required to appraise and set aside that property which qualifies for exemption.

(2) If the taxpayer objects at the time of levy to the valuation of the property excluded by the Service, the assistance of three disinterested parties will be secured to determine the value of the property. See IRM 5314.1:(4) for further information.

ERRONEOUS, WRONGFUL, AND EXCESSIVE LEVY ACTIONS

(1) When it is determined that a notice of levy has been served in error, a copy of the release of levy and Pattern Letter P-548 (letter of apology) will be sent to the injured party. See IRM 5329:1(1)(a).

(2) In cases of wrongful levy, the property levied upon will be returned to its rightful owner or a refund made under the provisions of IRC 6343. SeeIRM 5347.4.

(3) In instances where improper levy action results in excessive collection, immediate steps will be taken for the initiation of the manual refund. See IRM 5374.5.

RIGHT TO REFUSE ENTRY

Taxpayers have the right to refuse Service personnel entry onto the private areas of their personal or business premises. See IRM 5342.

RIGHT TO REDEEM

(1) Taxpayers have the right to redeem levied property any time prior to sale by paying the full amount of tax and additions thereto, along with any expenses or costs in connection with the seizure and contemplated sale. See IRM 5345.2.

(2) Owners of any real estate sold, their heirs, executors, or administrators, or any person having any interest therein, or a lien thereon, or any person in their behalf is permitted to redeem the property sold, or any particular tract of such property at any time within 120 days after the sale. See IRM 5372 for computation of the 120 day period and the redemption amount.

RIGHT TO FILE A CLAIM FOR REFUND OR CREDIT

(1) Taxpayers have the right to file a claim for refund or credit if they believe their tax bill is erroneous or excessive.

(2) The claim can be initiated by the submission of Form 1040X, Form 1120X, Form 843, or such other form as is appropriate for the type of refund claimed.

(3) If a claim for refund or credit is rejected or no determination is made within six months, the taxpayer has the right to file a suit for refund in a U.S. District Court or in the U.S. Court of Claims.

(4) Additional details of filing claims for refund or credit are contained in IRM 5374.4 and 5374.5.

RIGHT TO FILE A CLAIM FOR SURPLUS PROCEEDS

(1) The taxpayer is entitled to surplus proceeds from the sale of seized property unless another person establishes a superior claim.

(2) All claimants, including the taxpayer, must submit an affidavit to be considered in the distribution of the surplus proceeds.
(3) See IRM 5374.3 for instructions on the disposition of surplus proceeds.

STAY OF SALE

Property seized in connection with jeopardy or termination assessments may not be sold until expiration of the petition filing period with the U.S. Tax Court or until a final determination has been rendered by the Tax Court. See IRM 5213.25 and 5352 for exceptions and additional details.

RIGHT TO REQUEST REAPPRAISAL OF MINIMUM BID PRICE

A taxpayer is provided the minimum bid price prior to sale. If not in agreement, a Service evaluation engineer or a professional appraiser may be requested to assist the revenue officer in reevaluating the price. See IRM 5361.1 for minimum bid price procedures.

RECOMMENDATION #5:

IRC 6331(c), Sucessive Seizures, allows the IRS to levy upon any additional property after a previous levy has proven to be insufficient to pay the tax. Congress should amend IRC 6331(c) by adding the following at the end of paragraph C:

> ...except when such seizure is released to the taxpayer because the taxpayer has paid to the United States the value of the interest of the United States in the property, or because the value of the interest of the United States is insufficient to meet the expenses of sale, the Secretary will be prohibited from making a successive levy on that same property for the same liability under which the previous levy was made, for a period of at least 90 days.

Reasons for Change:

The current successive seizure statute is a *carte blanche* license to harass taxpayers by continuously seizing the same property after it has been released. This could occur when the revenue officer is under orders to "maintain pressure" on the taxpayer "until he gives in and pays." The successive seizure authority can be a vicious tool when used indiscriminately, or without regard for the personal effects it would have on the taxpayer.

Adoption of recommendation #3 would require the IRS to release seized property when the taxpayer pays the value of the U.S. interest in the property or when the value of the U.S. interest is insufficient to meet the expenses of sale. This proposal tightens up the successive seizure authority by requiring IRS to wait a reasonable length of time, 90 days, before again seizing the same property that had been previously released for either of the two given reasons. It is assumed that the 90-day interim period would be used by the IRS and the taxpayer to devise a constructive plan of action regarding the liability, and that should the taxpayer prove to be uncooperative and/or uncommunicative during that period, the right to make a successive seizure would only be allowed after the end of 90 days.

This restriction only applies to a previous seizure that had been released for the two given reasons. Seizures released for other reasons would not be restricted.

RECOMMENDATION #6:

Congress should include a subsection as part of IRC 6331 to read as follows:

> Recognizing that the fair and equitable administration of the internal revenue laws is important to voluntary compliance, the Secretary shall issue regulations specifying the circumstances, conditions, and situations under which a levy will be made.

Reasons for Change

In the January 1976 report of the Administrative Conference of the United States, entitled "Collection of Delinquent Taxes," it was pointed out that the IRS had no clear guidelines specifying when levy action was to be taken. The following is taken from page 96:

> The emphasis on numbers gives rise to more serious possibilities of abuse, such as the instances reported by Internal Audit of seizures of property in which the taxpayer was known to possess no equity. In each case the property was returned without payment of the tax. Such action exposes the Service to suggestions that it is misusing its powers and thus may tend to diminish voluntary compliance by the public — a damaging result for our self assessment system of taxation.
>
> Lacking guidance, revenue officers vary in their criteria for seizure of assets of individual taxpayers. Some told us that they will seize only when they expect to make forced sale of the seized assets. Other claimed to seize only when it was anticipated that the taxpayer would redeem the property. A few mentioned making seizures to impress the taxpayer with the serious consequences of not meeting his tax obligation. So long as the Internal Revenue Service fails to delineate clear purposes for the use of summary powers, we believe that these divergent criteria will continue to exist. The variations in practice may lead to the appearance of arbitrariness and caprice in some actions, thus undermining the taxpaying public's confidence in (and compliance with) the taxing system.

Two years after that report was issued, on July 31, 1978, the GAO issued a report entitled: "IRS Seizure of Taxpayer Property: Effective But Not Uniformly Applied." It reported that the decision to seize is made for different reasons in different districts, and pointed out that the IRS still did not have clear guidelines on when a levy or seizure should be made

In an internal memorandum to the Director of the Collection Division dated May 28, 1980, the Chief of the Evaluation and Research Branch stated that the:

> Statistics confirm a wide range of variation in the use of enforcement actions by individual districts. The variation does not appear to be random; rather, patterns of high frequency or low frequency tend to remain in specific districts over a number of years ... Levy actions are used by revenue officers in a multitude of conditions. *The Internal Revenue Manual does not specify conditions requiring levy or seizure actions.* It outlines some mandatory technical requirements and stresses efficient and fair employment of such tools. We rely heavily upon the independent judgment of the revenue officer. Of course, these judgments are not made in an influence-free environment. *Collection management can influence and monitor the revenue officer decisions.*

Hearings before the Senate Subcommittee on Oversight of Government Management of the Committee on Governmental Affairs on July 31, 1980, revealed that supervisory pressure to produce enhanced enforcement statistics resulted in intolerable abuses of taxpayers' rights, a disregard for the judicious exercise of the levy power, and numerous violations of IRS policies and procedures. In effect, various districts have contravened national policies with their own guidelines, written and unwritten.

It is necessary for the national office to ensure fair and equitable treatment of all taxpayers by issuing guidelines on the proper use of the levy powers. As it has been over six and one-half years since the situation was brought to light, this would suggest that the national office is not interested in meeting its responsiblities as the agency's chief policymaker, nor is it much interested in fulfilling its mission to provide "for the uniform interpretation and application of the tax laws." Since the IRS has not been responsive enough to issue seizure guidelines, Congress should direct them by statute to do so.

RECOMMENDATION #7

Congress should add a subsection to IRC 6334, Property Exempt from Levy, as follows:

> Any amounts received by an individual otherwise qualifying for exemption under subsection (a)(9) of this Section, deposited in a financial institution, shall be subject to the same exemptions as specified in subsection (d) of this section. Any levy upon the deposit(s) of wages, salary, or other income shall not be continuous.

The Tax Reform Act of 1976 amended IRC 6334(a) by providing a minimum exemption from levy for wages, salary, and other income "payable to or received by an individual."

The regulations pursuant to IRC Section 6334(a)(9) clearly ignore the meaning of the words "received by" and, in fact, clearly restrict the minimum exemptions to "only wages, salary, or other income payable to the taxpayer after the levy is made on the payor. No amount of wages, salary, or other income which is paid to the taxpayer before levy is made on the payor will be exempt from levy."

The regulations even provide an example establishing the fact that wages, salary, or other income already received by an individual and deposited into an account at a financial institution *do not* qualify for the minimum exemptions. The following example appears under subparagraph (b) of the IRC section 6334:

> Example. Delinquent taxpayer A, an individual is employed by the M Corporation and is paid wages on the first and fifteenth day of each month. Accordingly, A is paid wages on Monday, August 15, 1977. On Wednesday, August 17, A deposits these wages in his personal checking account at Bank X. On Friday, August 19, levy is made on the M Corporation and also on Bank X. Amounts payable to A as wages on September 1, 1977, and any payday thereafter may be exempt from levy under section 6334(a)(9). No amount of the wages A deposited in his account at Bank X on August 17, 1977, are exempt from levy under section 6334(a)(9).

The IRS's position is that wages, salaries and other income are changed in character once they've already been paid to, or, in essence, already received by the taxpayer. Otherwise, why would they deliberately not apply IRC 6334(a)(9) to deposits in a financial institution that originated from wages, salary, or other income? The unanswered question, then, is what is the meaning of the words "received by" in IRC 6334(a)(9)?

This proposal would clarify that unanswered question by applying the minimum exemptions to the same wages, salary, or other income already received by the taxpayer as are applied to those wages, salary, or other income payable to the taxpayer.

RECOMMENDATION #8:

Congress should adopt the following provision related to seizure action:

> The Secretary shall be prohibited from making a levy where it is apparent at any time prior to seizure that the value of the U.S. interest in the property is insufficient to meet the expenses of seizure and sale.

Reasons for Change:

This provision would protect taxpayers from harassment seizures or seizures made merely to "teach the taxpayer a lesson." The Internal Revenue Manual prohibits this kind of activity, and codifying the prohibition would help to guarantee compliance.

RECOMMENDATION #9:

Congress should adopt the following provision related to seizure action:

> The Secretary shall have no authority to make a levy upon any of an individual's property during the day the individual is in compliance with a summons issued under IRC Section 7602, unless collection of the tax is deemed to be in jeopardy.

Reasons for Change:

Some revenue officers have abused the summons authority by seizing the taxpayer's automobile parked in the parking lot outside the IRS office while the taxpayer was inside the IRS office complying with the summons. This section would prohibit that type of abusive behavior.

RECOMMENDATION #10:

Congress should amend the second line of IRC 6331(a) by replacing the words "within 10 days after notice and demand" with the words "within 30 days after notice and demand." The first two lines of IRC 6331(a) will then read:

> If any person liable to pay any tax neglects or refuses to pay the same within 30 days after notice and demand, it shall be lawful for the Secretary to collect such tax. . . .

Reasons for Change:

The 10-day notice and demand period is not reasonable for a taxpayer who needs to borrow the money or raise cash in some way. Thirty days is more reasonable.

As a practical matter, because of the IRS notice process, where three or four notices are sent to taxpayers over a 12 week period, very few levies are made within 30 days of assessment. The levies that do occur within this period are usually related to unpaid employee withholding taxes, and usually where the revenue officer has obtained a voluntarily filed form 941 and has promptly assessed the tax. Revenue officers frequently threaten to seize a taxpayer's business within hours of obtaining an immediate assessment, thereby illegally invoking the jeopardy authority under IRC 6331(a), using the fact of the delinquency itself as evidence that collection of the tax is in jeopardy. Then, in order not to break the law, the revenue officer waits 10 days and then seizes. Once the wheels are in motion to seize, the revenue officer will not withdraw from the process for any reason other than full payment. A rapid seizure may actually jeopardize collection itself by making it more difficult for the taxpayer to borrow money to pay the tax. Private and commercial lenders may then be reluctant to lend money for a business already under seizure by the IRS.

RECOMMENDATION #11:

Congress should adopt the following provision as a restriction upon the levy power:

> The Secretary shall not levy, except with the written approval of the

District Director or Assistant District Director without further delegation, or excepting where collection of the tax is in jeopardy, or excepting where "exigent circumstances" compel such a levy, the following:

(1) The real property used by the taxpayer, other than a corporation, as a principal place of residence year-round.

(2) The automobile used by the taxpayer as the primary source of transportation to and from his place of business or employment.

(3) The tangible personal property of the taxpayers business, other than a corporation, when the levy of such property may result in the closure of the business.

Reasons for Change:

The levy power of the IRS is a far reaching authority. As we have seen, some revenue officers and some collection managers take this power too lightly; they are irresponsible in their administration of this authority.

Next to criminal enforcement, distraint action is the most sweeping action that adversely affects the most taxpayers. The Service cannot allow its collection managers to view their responsiblity lightly or as a means of expressing their own peculiar "masochism." In order to prevent overzealous enforcement, levy or seizure action on a taxpayer's residence, his primary source of transportation, or his business assets should only be an "agency decision," not the decision of one collection employee.

RECOMMENDATION #12:

Congress should adopt the following provision as a procedural requirement for levy:

> The Secretary shall either send by certified mail or registered mail, or hand deliver in person or by leaving at the dwelling or usual place of business, of such individual, a written Notice of Intent To Seize within the 10-day to 30-day period preceeding the date of levy, unless collection of such tax is in jeopardy. Such notice will notify the taxpayer of the levy provisions of the Code, administrative appeal procedures prior to levy, and possible alternative collection remedies available to the taxpayer, such as installment agreement, Offer in Compromise, and suspension of collection due to hardship. This notice shall also serve as the same notice specified in Section 6331(d)(1).

Reasons for Change:

In its July 1978 report, "IRS Seizure of Taxpayer Property: Effective, But Not Uniformly Applied," the GAO reported that 25% of the taxpayers they interviewed were not aware of IRS's seizure authority. Furthermore, 57% said they were not told that seizure was the next action to be taken. The GAO felt that "informing taxpayers about these powers and that seizure is the next action might reduce seizures," and thereby "save both IRS and the taxpayers time, trouble, and expense."

Taxpayers currently have the right, under an *informal* process, to appeal a revenue officer's decisions concerning payment options proposed, a rejection of an offer in compromise, or the decision to seize. When taxpayers reach an impasse with revenue officers regarding their ability to pay, IRS guidelines provide that taxpayers be given an opportunity to request a review by a group manager (IRM 53(10)2).

If taxpayers do not request a higher level review of their case, revenue officers are supposed to inform them of their right to appeal. However, the GAO discovered that revenue officers were not following those instructions in some districts, and recommended that revenue officers in all districts need to substantially improve their performance in advising taxpayers of this right.

RECOMMENDATION #13:

Congress should grant certain taxpayers the right to file suit in a federal District Court subsequent to levy by adopting the following provision:

> A taxpayer may file suit in a U.S. District Court, prior to levy, to enjoin the Secretary from making a levy, or subsequent to levy to enjoin the Secretary from selling such property levied upon, and to obtain a release of levied property by reasons that: the deficiency assessment was made without knowledge of the taxpayer and without benefit of the appeal procedure; or there has been an improper or illegal assessment; or there has been an action in violation either of the statutory procedures of the Tax Code, the policies or regulations of the Internal Revenue Service, or the procedural requirements of the Internal Revenue Manual providing taxpayer safeguards; or the Secretary has made an unlawful determination that collection of the tax was in jeopardy pursuant to Section 6331(a); or the value of seized property is out of proportion to the amount of the liability, and other collection remedies are available; or the value of the U.S. interest in the seized property is insufficient to meet the expenses of seizure and sale; or the Secretary will not release the seized property upon an offer of payment of the U.S. interest in the property; or the Secretary has arbitrarily established a minimum bid price on the seized property in such a way as not to preserve or protect the taxpayer's equity in the seized property.

Reasons for Change:

Under IRC 7421 no suit can be brought by any person in any court for the purpose of restraining the assessment or collection of any tax, except as provided in sections: 6212(a), relating to notice of deficiency; 6213(a), relating to the 90-day letter; 6672(b), relating to suits for determining liability of the 100% penalty; 6694(c), relating to liability of preparer penalty; 7426(a), relating to wrongful levies; 7426(b)(1), relating to irreparable injuries to superior rights of the U.S.; and 7429(b), relating to appeal of jeopardy assessment procedures.

The case law pertaining to Section 7421 indicates a myriad of problems in obtaining injunctions to restrain the collection of the tax. It is clear that injunctions will be granted where the failure to grant relief would result in irreparable damage to the taxpayer. But an injunction will only be allowed where it is clear that under no circumstances would the government prevail. Otherwise, only two remedies are available to the taxpayer: (1) pay the tax, file a claim for refund, and sue for recovery if the claim is rejected; (2) file a Petition in Tax Court before assessment and within the short period of time allowed for filing such petition.

Taxpayers' rights should be protected in other ways, and Section 7421(a) should be amended to provide for such protection. The issues enumerated in the proposal pertain mostly to the application of the levy statutes in a way that may have as much of a detrimental or deleterious impact upon taxpayers as the illegality or irreparable injury issues.

RECOMMENDATION #14:

Congress should adopt a provision to allow taxpayers to administratively appeal a decision of the Collection Division to file a Notice of Federal Tax Lien when such filing would hamper or jeopardize collection of the tax.

Reasons for Change:

IRM 5426.1:(1) allows revenue officers the discretion to decide not to file a Notice of Federal Tax Lien when "the filing of a notice of lien would hamper collection." The revenue officer is supposed to be free to make his nonfiling decision if the balance due is under $2,000, and he is not even required to record the reasons why in the history sheet. If the case is between $2,000 and $5,000, the revenue officer must record the reasons for the nonfiling in the case history sheets, and no managerial approval is necessary (according to the IRM but some districts give the group manager approval authority anyway). Approval for nonfiling is required only when the case is over $5,000.

It was revealed during the Levin hearings, and I know this to be a fact, that in many districts revenue officers file Notices of Federal Tax Liens without regard for what it may do to the taxpayer's ability to borrow the money to pay the taxes. There are times when it is absolutely necessary that the tax lien *not* be filed in order not to disturb the ability of a financial institution to advance funds to the taxpayer. The issue of tax lien priorities is a very complex one often requiring litigation to untangle. Lenders are sometimes reluctant to advance funds to delinquent taxpayers unless they can be assured the IRS will not immediately enforce its lien priority, thereby putting the taxpayer out of business and jeopardizing the lender's chances of recovering the loan.

Revenue officers also testified during the Levin hearings that some group managers or branch chiefs would frequently deny their requests for nonfiling of the tax lien for no apparent reason. While this arbitrary enforcement philosophy is used by these managers on the pretext of protecting the government's interest, in fact they are actually jeopardizing the government's potential to collect tax money in the most efficient way. There are times when the government can collect more by helping the taxpayer work through his difficult periods and stay in business than by putting him out of business and selling his assets at nominal value. Sometimes the nonfiling of a tax lien is crucial to preservation of the business.

Taxpayers who can provide evidence that the filing of a Notice of Federal Tax Lien would hamper the collection of the tax ought to be able to administratively appeal the decision to file. Naturally, the appeal should be made outside of the Collection Division to an impartial source like the Ombudsman (more specifically the PRP officer) who could issue a Stop Action Order to temporarily delay filing the lien.

RECOMMENDATION #15:

Congress should require the IRS to issue a "Miranda-type" warning to taxpayers during any interview in connection with the assessment of a deficiency. The taxpayer should be warned that he has the right not to disclose any information or evidence that he believes would violate his Fifth Amendment rights against self-incrimination, that any such information or evidence would be used against him, and that he has the right to the presence of an attorney, a CPA, or an enrolled agent during the interview or examination.

Reasons for Change:

An audit is a civil procedure even though it can be the prelude to a criminal investigation and courts in the past have not applied the Miranda warnings to civil procedures. A taxpayer can be caught in a different situation: he has no choice but to cooperate with the tax auditor, unless he is willing to subject himself to any amount of additional assessment that the IRS might otherwise propose.

A taxpayer who cooperates with the IRS, and who has committed no fraudulent act, only incurs the possibility of additional tax assessments, interest, and various civil penalties. A taxpayer who cooperates with the IRS and who has committed a fraudulent act, subjects himself to possible criminal prosecution by self-incrimination.

Any taxpayer who does not cooperate with a tax auditor or revenue agent immediately arouses suspicion. The auditor can decide to either summons the taxpayer's books and records or to refer the case to the Criminal Investigations Division to determine if there is the potential for a fraud prosecution. Either way the taxpayer loses because a federal judge can require the taxpayer to produce the books and records under threat of contempt of court, and the Criminal Investigations Division might "scare" the taxpayer sufficiently to comply. The taxpayer might well imagine the IRS making a fraud case of a situation that was not initially intended to be.

But taxpayers do need to know that any normal, routine civil audit may lead to a potential fraud investigation which may turn into a criminal prosecution. The Fifth Amendment protection against self-incrimination should give a taxpayer the opportunity to decide if he will cooperate. The penalty for a contempt of court citation may be preferable to the penalties levied for fraud. At any rate, a lot of IRS's criminal prosecutions are successful because they are able to obtain evidence granted to them through the initial cooperation of the taxpayer.

The IRS is concerned that giving taxpayers the Miranda warnings will unnecessarily frighten and worry them. Taxpayers have seen it on TV a million times; the warnings are always given to the criminal as he's being hauled off to jail. This perception will certainly cause many "honest" taxpayers to be more concerned than they need to be. While the intention of the safeguard warning provision is to expand the rights of taxpayers, in doing so it actually instills such fear of the IRS that it could actually result in a severe detriment to them. After being audited once and subjected to the Miranda warnings, honest middle-class taxpayers may then decide to take fewer deductions than they would normally take or be entitled to, with the explicit intention of avoiding an audit.

I believe that there is a way to fulfill the need of taxpayers to know, to maintain their Fifth Amendment rights, and yet not frighten them needlessly. The Congress should consider the adoption of a statement that conveys a message that is instructive and protective, but not overbearing, harsh, or frightening. It could be something like this:

> This examination of your tax return is intended for the civil administration of the tax laws of the United States. In order for us to perform this function properly, we need your cooperation. But you should know that in the event we find evidence that appears to indicate a criminal violation of the tax laws, the scope of this audit examination will change from civil to criminal. If that happens you will be notified. Anything you tell us or any books and records you give us during the course of this audit examination may later be used in the investigation of the alleged criminal violation. For this reason you have the right not to disclose any information or evidence that you believe would violate your Fifth Amendment rights against self-incrimination; any such information or evidence may be used against you, and you have the right to the presence of an attorney, a CPA, or an enrolled agent during this interview, or examination.

RECOMMENDATION #16:

Congress should require that an Office of Ombudsman be maintained within the IRS, and should provide that the Ombudsman be appointed by the President for a four-year term.

The Ombudsman should have the right to intervene in any enforcement proceeding or activity when a taxpayer has made a petition to the Ombudsman that at least one of the following conditions exist:

- There has been an improper or possibly illegal assessment.
- There has been an assessment made without the knowledge of the taxpayer and without benefit of the taxpayer's appeal rights.
- There has been an action in violation either of the statutory procedures of the Tax Code, the policies or regulations of the IRS, or the procedural requirements specified in the Internal Revenue Manual.

Reasons for Change

There already is an Ombudsman, who is on the Commissioner's immediate staff. The Ombudsman "administers the Problem Resolution Program nationwide, represents taxpayer's interests and concerns within the decision-making process, reviews IRS policies and procedures for possible adverse effects on taxpayers, proposes ideas on tax administration to benefit taxpayers and represents taxpayer's views in the design of tax forms and instructions." (Commissioner's Annual Report, 1981.)

The Taxpayer Ombudsman position was established pursuant to Executive Order 12160 of September 26, 1979, ("Providing for Enhancement and Coordination of Federal Consumer Programs") in order to strengthen and enhance the already existing Problem Resolution Program, established in 1977.

The Ombudsman should be a political appointee and not a career IRS employee. As a political appointee the Ombudsman would be free to be a true taxpayer advocate without worry for his career aspirations within the IRS. He would not have to worry about how other IRS managers feel about his input into their areas of responsibility. Also, a political appointee would come to the job independent of the restrictive mission-oriented mentality that besets so many career executives. Not being engraved with IRS philosophy and methods of operation, he should be more perceptive to the needs of taxpayers and more receptive to changing the old ways of doing things. A four year term would enable each new administration to replace the Ombudsman according to its needs.

The IRS has expressed some concern about the Ombudsman being a political appointee. Commissioner Egger has testified that such independent power would not provide a balance between protecting the government's and taxpayers' interests and would open up dangerous potential for political abuse of the tax system." It is questionable that those arguments really hold water. After all, the Commissioner is a political appointee. I'm convinced that there is room in the IRS for another political appointee. (The Commissioner is presently the only political appointee in the entire agency.)

RECOMMENDATION #17:

Congress should provide for a judicial appeal of a levy made without regard for the 10-day notice and demand requirement as allowed under IRC 6331(a) when collection of the tax is deemed to be in jeopardy.

Reasons for Change:

There are two types of jeopardy situations: when collection of the tax is in jeopardy under IRC 6331(a), and when the assessment or collection of a deficiency will be jeopardized by delay under IRC 6861 or IRC 6862. (IRC 6861 involves income taxes; IRC 6862, all other taxes.) The provision under IRC 6331(a) involves immediate collection when the taxpayer has voluntarily filed a tax return, and the provisions under IRC 6861 and IRC 6862 normally refer to either a deficiency found in an audit examination or to the circumstance in which no tax return was filed. The Tax Reform Act of 1976 provided for administrative appeal and judicial review for assessments made under IRC 6861 and IRC 6862. There are presently no known problems with the administration of IRC 6861 and IRC 6862.

Problems do arise, however, under immediate collection procedures (the IRS refers to them as "prompt assessments") in the jeopardy clause of IRC 6331:(a). The applicable IRM sections follow:

Prompt Assessments
5213.4

GENERAL

(1) Prompt assessments are generally only requested when a taxpayer voluntarily files a delinquent or current tax return as the result of a delinquency investigation or a return compliance program. When a taxpayer refuses to file a return, and collection of the tax liability is determined to be in immediate jeopardy, the procedures contained in IRM 5213.2 should be followed. For special provisions regarding 100 percent penalty cases and returns prepared and signed under authority of IRC 6020(b), see IRM 5213.45.

(2) Taxpayers who voluntarily file tax returns or who have exhausted their pre-assessment appeal rights on proposed 100 percent penalty or IRC 6020(b) assessments, are not legally entitled to any delay in the assessment of the amount of tax

indicated on the return. For purposes of administrative efficiency, tax returns are not normally assessed immediately upon receipt. Under the prompt assessment procedures, if collection of the tax is believed to be in jeopardy, the return is immediately processed and assessed. Then, collection of the tax is declared to be in jeopardy under the authority of IRC 6331(a). Collection action may then be taken without regard to the ten-day notice and demand period.

(3) It is important to emphasize the differences between a jeopardy assessment and a prompt assessment. A jeopardy assissment can only be approved by the District Director or the Director of International Operations. Jeopardy assessments are recommended when collection is deemed to be in jeopardy, and there is not sufficient time to assess the unagreed tax liability using standard procedures. A prompt assessment is made when collection is determined to be in jeopardy on a tax liability which can be assessed, i.e., when a return has been voluntarily filed, and when assessment appeal rights have been exhausted on a proposed 100 percent penalty or IRC 6020(b) assessment.

CRITERIA FOR RECOMMENDING PROMPT ASSESSMENTS

(1) The necessity for prompt assessment should be rare and should only arise in instances where collection of the tax appears to be in jeopardy at the time the delinquent return is secured or prepared and when there is every intnetion of proceeding with enforcement action immediately upon receipt of the assessment.

(2) Prompt assessments should be limited to the following situations and will be based upon the facts and circumstances of each individual case: a)taxpayers who are consistently suffering financial losses; b)taxpayers against whom large damage suits are pending, or against whom such suits are threatened; c)taxpayers who have a past record of resisting or avoiding payment of their taxes; (d)taxpayers suspected of having plans for leaving the United States without making provision for payment of their taxes, with particular attention being given to aliens; (e)other taxpayers, where the facts and circumstances indicate that the taxpayer's present or future financial condition is such as to make collection of the tax doubtful.

(3) Since the initial decision as to whether or not collection of a tax is in jeopardy must be made by the person handling the case, it is necessary that proper authority be delegated to that person. District Directors and the Director of International Operations should consider issuing redelegation orders authorizing revenue officers, GS-9 and above, to enforce collection without regard to the ten-day notice period on any case where it is determined that collection of the tax may be in jeopardy.

(4) If the initial investigation indicates that collection may be in jeopardy and the investigating employee does not have delegated authority, the case should be discussed with a revenue officer who has been delegated the authority in (3) above, and a decision should be made as to the course of action to be made.

(5) The case history file should be fully documented to reflect the facts and circumstances that support the determination that collection is in jeopardy, e.g., Collection Information Statement, financial analysis, narratives of conversations with other creditors of the taxpayer, data on previous case histories, or other list of leviable assets upon which enforcement action may be taken when assessment is received.

STATEMENT OF THOMAS J. DONOHUE, PRESIDENT, CITIZENS CHOICE, WASHINGTON, D.C.

Mr. DONOHUE. Thank you, Mr. Chairman. As is the case, we will also submit a statement for the record.

It is interesting to note that, to the best of my knowledge, the participants of this panel, having gotten together before this presentation to organize their materials, how much we feel the same in terms of the tens and tens of thousands of people that we represent.

Citizens Choice represents 75,000 taxpayers, and, as you know from many of the previous opportunities we have had to discuss this matter, they are very active in the question of the relationship between the IRS and the individual taxpayer.

You will recall that back in 1981 we finished a year and a half long study of this question through the mechanisms of a National Commission on Taxes and the Internal Revenue Service, and we published what has proved to be a useful and provocative document for both the Congress and the IRS to address these issues.

We found in that study that the adversarial relationship between the taxpayer and the IRS was contributing significantly to the sort of mentality that "I just won't pay," and that if we didn't do something over a short period of time, the underground economy—as has already been suggested here today—would grow rapidly, and the number of people that voluntarily complied with the tax system would diminish. And that was not because we have a nation of criminals; it is because we have a nation of people that dealt with a complicated, convoluted system that frightened them to death. They didn't understand it.

I submit, sir, if you went around the floors of the Congress where there are plenty of lawyers, you will find a lot of people who don't understand it, as well.

And so came with that concern, that inability to understand the system, a mentality of fear.

We were very encouraged last year when the Congress moved forward "to begin the process"—and I repeat, "to begin the process"—of protecting the rights of the taxpayers. And you get much of the credit for that movement in the right direction.

I think the attorneys fee issue, the question of notice before seizure, informing taxpayers of their rights, which hasn't quite happened yet, were all in the right direction; but, as has already been suggested, there are a number of things that we must do here to make that a meaningful change.

First of all, I think, as in any of our systems of government, we ought to put the burden of proof on the IRS on the question of attorneys fees. I mean, it is interesting for a taxpayer to basically beat the IRS in court and then have to go out and say, "Well, we were right and you were wrong. You should pay the fees." I think it ought to be the other way, as you have expressed on other occasions.

I think we ought to have a third party, whether it be somebody appointed by the Treasury Department, whether it be judges, whether it be someone else, who determines when seizure can take place before it takes place.

I have just an innate problem about putting the fox in charge of the chicken coop, and I think we need to move forward and have some protection in the matter of seizure beyond what has already been legislated.

And finally, sir, I would like to mention a little something about the question of amnesty.

We have come on the amnesty issue through another approach, and I would like to mention it to you. One of our other organizations at the U.S. Chamber of Commerce is the National Chamber Foundation. They are doing a massive study on the Hispanic business community. One of the things that they have found out is that there are a large number of entrepreneurs who started years ago in mom and pop businesses and have grown, but who are retaining their growth because when they got started they never got into paying income tax. And they would like to pay taxes. But they are frightened that the minute they come forward and start to do that, that they are going to be in deep trouble.

I would suggest that we just expand our thinking a little bit beyond the criminal prosecution issue and understand that maybe we can find an amnesty for those who have never paid taxes—not for those who have been in and out of the system for their own advantage, but for those who have never paid, who have never had an opportunity to participate. And we might do ourselves a great deal in an amnesty system to get people back in the system if it is accompanied by some simplification.

Let me and my comments in that regard.

As you know, Citizens Choice went further from its study and began to encourage the debate on the tax simplification system. And you have participated, as have others, in our national forums on that subject. It is absolutely essential that that debate continue.

There are two or three schools of thought, of course. There are those who want to simplify the system to collect more money from the taxpayers to have more Government.

There are those who would like to simplify the system, on the other hand, to get more people to participate in the system, to make it fair and equitable for everyone.

We need to get those people in the room, we need to keep that discussion going, because the citizens of this country will only pay the taxes so long as it appears to be fair, reasonable, and equitable. And if we don't continue to fight to protect their rights and to give that perception, they will all go, sir, on a holiday.

My final thought is that we would encourage your efforts to get some additional money for the IRS for training and for additional agents, not because we encourage more agents to go out and audit more people, but better trained, better staffed, better managed IRS system, and we will have fewer complaints.

I thank you very much, Mr. Chairman. As always, our staff as well would be very happy to help. As you know, Mr. Lynch is up here often with your colleagues, and we will do anything we can to help you move this project forward.

Senator **Grassley**. Thank you.

[The prepared statement of Thomas Donohue follows:]

STATEMENT OF THOMAS J. DONOHUE, PRESIDENT, CITIZENS CHOICE, INC.

I am Thomas J. Donohue, President of Citizen's Choice, a national grassroots taxpayers' organization founded in 1976. Citizen's Choice has presently over 75,000 taxpaying members nationwide, representing all sectors of our society.

I am pleased to have this opportunity to testify before this committee on the relationship between the taxpayer and the Internal Revenue Service. Citizen's Choice is well qualified to present testimony on this subject having made a year and a half long investigation into this relationship through the National Commission on Taxes and the I.R.S. One of the major conclusions of this study which was completed in 1981 was that the relationship between the taxpayer and the Internal Revenue Service was becoming increasingly adversarial. This situation was aggravated by an overwhelmingly complex tax system which is both frustratingly difficult to administer and beyond the competence of many taxpayers to comply with. The Commission concluded that unless something was done to improve the taxpayer/I.R.S. relationship and to radically simplify the system that our system of voluntary tax compliance would eventually collapse of its own weight.

We are happy to report that since the issuance of the Commission's final report, positive steps have been taken to improve the relationship between the taxpayer and the I.R.S. In particular, last September the Congress enacted a number of taxpayer rights long advocated by Citizen's Choice. This legislation, which was incorporated in the 1982 Tax Bill, brought taxpayers within the purview of the "Equal Access to Justice Act" by allowing the award of court costs and attorneys fees in certain circumstances; required that the I.R.S. provide notice to a taxpayer by certified mail prior to the seizure of property; considerably increased the dollar value of property and wages exempt from seizure and of significance to the largest number of our citizens, provided that the I.R.S. make every effort to fully and fairly inform the taxpayer of his rights prior to the conduct of an audit.

The tax simplification effort is also gaining speed. Three "National Forum on Tax Alternatives" have been sponsored by Citizen's Choice and have promoted an active dialogue on the very complicated question of simplifying the American tax system. In this regard, we urge the members of the Finance Committee to actively consider the question of tax simplification through additional congressional hearings during the 98th Congress provided that any simplification results in an actual tax decrease. It is our opinion that simplifying the tax system is the single most important step in solving the compliance problem. While we may be successful in promoting the debate, only Congress is capable of bringing about the necessary changes.

We recognize, however, that any major simplification of the tax code will not occur overnight. Nevertheless, we believe that there are smaller steps that can be taken to improve the taxpayer/I.R.S. relationship. The reforms enacted last year will pay dividends in an improved voluntary system of compliance. The relationship could be further improved if Congress and the I.R.S. adopt these additional recommendations of the Commission:

1. Congress should be responsive to I.R.S. budget requests that reflect its need for increased levels of agent training and experience thus enabling the I.R.S. to impose higher threshold requirements, to intensify existing training programs and to make existing pay scales competitive. The Internal Revenue Service should not have to operate under a continuing resolution, especially since every dollar budgeted results in four to five dollars additional revenue.

2. Both the Congress and the Internal Revenue Service should seek a relaxation of substantiation requirements in many areas to ease the burden and expense of voluminous record keeping and in situations where there is no reason to suspect fraud. Detailed substantiation requirements punish the innocent without apprehending the guilty.

3. Congress should increase the number of "safe harbor" tax provisions in the areas where precise figures are difficult to substantiate. Such provisions, because of their inherent certainty and patent fairness, are immensely popular with the taxpaying public, especially since the establishment of the "safe harbors" is an excellent, easily understood opportunity for public participation and compromise.

In addition to these recommendations, Citizen's Choice urges Congress to improve on two of the reforms enacted last year and to seriously consider solutions to the problem of non-filers.

In the former area, Congress should strengthen the attorney's fees provision by allowing an award to a taxpayer litigant unless the position of the I.R.S. was substantially justified. This would place the burden of proof on the I.R.S., which is more likely to have the facts at hand to justify the litigation than the taxpayer, who under current law must prove the I.R.S. position unreasonable.

The requirement that the I.R.S. must send a notice of seizure by certified mail was an improvement. However, it fell short of the independent third party review that a court order prior to seizure would provide. We believe that any additional expense incurred by the I.R.S. by such a requirement could be handled through increased budgetary allocations. We also are convinced that this reform would do more to improve the image of the I.R.S. than all potential and existing reforms combined. An improved image will result in improved compliance.

We encourage the consideration of amnesty for those citizens who have never filed a tax return. The research of the National Chamber Foundation, an affiliate of the U.S. Chamber, indicates that there exists a high incident of non-filers in the Hispanic business community. It is first a lack of knowledge that causes the failure to file and then the fear of penalty that prevents subsequent filings. This is one reason which accounts for the slow growth of this segment of American business. We are equally certain that other businesses and individuals are similarly situated. A one time only forgiveness of legitimate non-filers, not individuals or businesses who have quit the system, would generate billions of dollars in additional revenue.

Citizen's Choice would like to commend the efforts of the I.R.S. to simplify forms and clarify accompanying literature. In particular, we understand that the 1982 "EZ Form" has been an overwhelming success in the number of taxpayers using this form over the 1040A. The Service should also be commended for the continuance of various taxpayers assistance and education programs despite having to operate under a continuing budget resolution. Citizen's Choice has found these programs to be important elements in an improved taxpayer/I.R.S. relationship.

One final point need be mentioned. There remains widespread ignorance on the part of taxpayers concerning the scope of their rights during an I.R.S. audit and the limitations placed on the powers of the examining agent. This suggests that current I.R.S. procedures for informing taxpayers of their rights may not be adequate. Last year, in response to this problem, Congress requested the I.R.S. to prepare an understandable list of the rights and responsibilities of a taxpayer and the auditing agent during the course of an audit. We understand that this process is ongoing and offer our assistance in whatever way it may be of help.

In addition, I offer to this committee and to any of its members in particular, our assistance in any way you might find it helpful towards reaching our common goal of an improved relationship between the taxpayer and the Internal Revenue Service. We look forward to working with you to this end.

STATEMENT OF ROBERT CAPOZZI, POLICY ANALYST, NATIONAL TAXPAYERS LEGAL FUND, WASHINGTON, D.C.

Mr. **Capozzi.** Thank you, Mr. Chairman, for the opportunity to testify this morning.

My name is Robert Capozzi, and I am the policy analyst for the National Taxpayers Legal Fund, a grassroots taxpayers' advocacy group with over 30,000 sponsors nationwide. Our chairman is former Senator Eugene McCarthy.

Our organization is very concerned about this issue of reducing taxpayers' burdens. We believe that taxpayers' rights are perhaps the most important issue to all Americans, since each of us is affected by the IRS as opposed to other Government programs. And of course we believe that the tax system should be fair and equitable.

Unfortunately that perception is not seen now. Many people see the IRS as something of a new Gestapo, and we believe that we've got to change that, and we've got to do something about that soon.

Part of the problem as we see it is that the issue and the debate in Washington has shifted from reducing the size of the Federal budget to this notion of revenue enhancement. We believe that revenue enhancement naturally tends toward what are called compliance measures, which we saw borne out in TEFRA.

Now, TEFRA, of course, did have some good aspects to it; but the compliance measures in TEFRA will only tend to increase the friction between the IRS and the taxpayers. One compliance measure in particular, withholding of interest and dividends, has already been repealed by an overwhelming majority—91 to 5 in the Senate, and 382 to 41 in the House.

We believe that this is an example of how the little guy has reached down and told the Congress that he does not want these further compliance measures.

What we believe that Congress should be moving toward is tax simplification, not further tax complication. And the best way to do that is through some sort of flat-rate tax system. This doesn't necessarily mean it would have to be a pure form. We see things like the Bradley-Gephart plan as being valuable; DeConcini's bill is good. The major thing that we see is good with the flat-rate tax is that it draws people out of the underground economy. If your goal is to broaden the tax base, the best way to do it is through a flat rate.

Now I would like to discuss some of the issues that Mr. Wade has put in "The Power to Tax," the book which we published, the last chapter of which I'd like to insert into the record at this time.

The vast majority of recommendations which we are putting forth in the book involve the seizing and levying powers of the IRS. For instance, currently the IRS can seize everything a taxpayer owns, up to 1,500 dollars' worth of his possessions. We believe that this figure was based upon a 19th century precedent, and that it should be updated. It should be more in the line of $20,000.

Furthermore, the IRS is very inflexible in regard to tax repayment. We believe that if a taxpayer shows that he has good faith, that he wants to pay his taxes and he is willing to do so, that the IRS should not be in the business of collecting retribution, but instead should try to be as flexible as possible in allowing the taxpayer to pay his taxes.

Similarly, frequently the IRS will seize property which the taxpayer could use and would use to facilitate his ability to pay those taxes back. The IRS should keep this in mind when they consider levying any of the taxpayers' properties.

Furthermore, and perhaps our most important recommendation, we believe that the Congress should come forth with a new taxpayer and third party rights section in the IRS code. We believe that the taxpayer should have the right to appeal to supervisory employees of the IRS, and conceivably should be able to go to a district problem-resolution officer.

Furthermore, taxpayers should be advised as a matter of course that they have these rights of appeal.

One thing that quite amazes me, sir, is the fact that the IRS currently has no guidelines in specifying the circumstances, conditions, and situations under which a levy will and can be made. This ought to be rectified. The code should be updated in order to reflect this.

My last major recommendation is that a new definition for the Office of Ombudsman should be made. The Ombudsman should be a political appointee of the President and should have the power to intervene in any enforcement proceeding.

I would like to conclude my statement by saying that I would hope the Senator would look at "The Power to Tax" and our recommendations in that.

Thank you very much.

[The prepared statement follows:]

STATEMENT OF ROBERT CAPOZZI, POLICY ANALYST, THE NATIONAL TAXPAYERS LEGAL FUND.

I want to thank you, Mr. Chairman, for the opportunity to testify this morning. My name is Robert Capozzi and I am a policy analyst for the National Taxpayers Legal Fund, a grassroots taxpayers advocacy group with over 30,000 sponsors nationwide. Our chairman is former Senator Eugene J. McCarthy. Our organization is very much concerned about the issue of how to reduce taxpayer burdens and with taxpayers' rights in general.

We at the Legal Fund believe that the issue of taxpayers' rights is of great importance to all Americans. Our revolutionary beginnings were founded upon a taxpayer revolt, one which was in response to capricious and arbitrary taxation. In order for the government of the United States to operate with the support of the American people, the one agency with which we all must deal -- the Internal Revenue Service -- should not act as King George did. The American tax system should be as fair and evenhanded as possible.

However, the fact of the matter is that the IRS is seen by many Americans as nothing short of a new Gestapo. This perception must be dealt with by Congress.

Part of the problem is the level of debate in Washington. Unfortunate as it may be, the debate in Washington has shifted away from the size of the federal budget to thinking of new "revenue enhancement" techniques. And when the issue of revenue enhancement comes up, the notion of tougher compliance measures inevitably enters the discussion.

The Tax Equity and Fiscal Responsiblity Act of 1982, known as TEFRA, was an example of questionable revenue enhancement. The increased compliance measures which were in TEFRA will tend to increase friction between the IRS and taxpayers. One compliance measure -- withholding of interest and dividends -- has already been repealed by overwhelming popular demand. The vote in the Senate was 91 to 5, and in the House 382 to 41. Withholding was as issue which hurt everyone, particularly the little guy, and so the public outcry for its repeal was heard far and wide.

The pro-taxpayer measures in TEFRA were seen as a positive development. However, they did not go far enough.

If there is a message from all of this it is that the American people want tax simplification, not further tax complications. Large numbers of people are now receiving some kind of professional help in preparing their income taxes. This is wrong. It is a wasteful and inefficient and unfair method of tax collection.

We at the Legal Fund have found that there is strong grassroots support for the flat-rate tax. If a pure form is impossible, then certainly a move toward tax simplification, like abolishing many tax preferences and reducing the number of income tax brackets, would be a step in the right direction.

However, even if we cannot get sweeping reform like the flat-rate, we have several suggestions on how to alter the present Internal Revenue Code in order to give the American taxpayer the same kind of rights that he has when he is involved with the criminal justice system. There are too many horror stories of the IRS running roughshod over taxpayers.

Of course, we believe that taxpayer assistance programs should be maintained, but we don't believe that the IRS budget should be increased. Instead, funds should be transferred from administrative and collection divisions to these assistance programs.

Now I'd like to devote the rest of my statement to specific changes in the IRS Code and IRS tactics which I believe are vitally important.

NTLF commissioned Mr. Jack Warren Wade, Jr., a former IRS agent and a co-author of the IRS training manual, to help us formulate about 20 recommendations which would help reduce friction between the IRS and the taxpayer. (I would like to insert the text of our book, The Power to Tax, by Mr. Wade, into the record, and to outline some of the recommendations which we spell out in the book.)

The vast majority of our recommendations involve the IRS's power of seizing and levying of the property an allegedly delinquent taxpayer.

For instance, currently the IRS can seize everything a taxpayer owns up to $1,500 worth or possessions. This paltry sum is primarily based on a 19th century precedent. It should be raised to $20,000.

Another problem is the IRS's inflexibility regarding repayment of taxes due. Once a taxpayer has had his salary levied by the IRS, the installment payment provisions should be made as flexible as possible. If a taxpayer's shows good faith in his desire to pay due taxes, the IRS should not be in the business of collecting retribution. Instead, the IRS should simply make sure that the taxes are paid.

Similarly, if there is property which the IRS wishes to levy, or has levied, and that same property in the hands of the taxpayer would facilitate the taxpayer's ability to pay his taxes, the IRS's levy should be released. The same is true in cases of financial hardship.

Once a taxpayer's property has been levied, the IRS should present the taxpayer with a written form saying that the taxpayer has the right of redemption of such property. Unfortunately, many taxpayers believe that once their property has been seized by the IRS, that the seized property is lost forever, which is not the case. This right should be made explicit by the IRS.

Perhaps our most important recommendation...We believe that a taxpayer and third party rights section should be added to the IRS Code. This section should include a strong statement to the effect that IRS employees have the dual responsibility to protect the interests of the IRS and to guard the rights of the taxpayer and third parties. Taxpayers should have the right to appeal to a supervisory employee of the IRS when their case reaches an impass with a collection employee. If necessary, the taxpayer should be able to go to the district Problem Resolution Officer. Taxpayers should be advised as a matter of course that they have these rights of appeal.

Excluded property which is levied by the IRS is to be appraised and evaluated by collection employees. If the taxpayer objects to these evaluations, three disinterested parties should be secured to make a determination on the value of the property.

In the case of a wrongful levy, the property should be returned to its rightful owner along with a letter of apology.

Taxpayers should have the right to refuse the entry of an IRS agent, unless a warrant is presented.

Taxpayers should have the right to file a claim for a refund or a credit if they believe that their tax bill is erroneous or excessive.

One problem which some taxpayers have encountered is that once their property has been seized in a jeopardy situation, the IRS has threatened to sell the taxpayers property before final determination has even been made in Tax Court. This is an option which the IRS should definitely not have. They are fallible, and if an innocent taxpayers property is sold off because of an IRS mistake, that taxpayer would have been unfairly victimized.

One IRS tactic which borders on harrassment is called "successive seizures." The IRS agent will make a seizure, release the taxpayer's property, and then seize it again.

We propose that a limit be put on successive seizures. We believe that a period of 90 days should elapse before another seizure can be made of the same property.

Amazingly, there are no real guidelines for the IRS specifying the circumstances, conditions, and situations under which a levy will be made. This ought to be rectified. In order to ensure that the IRS fairly and equitably deals with taxpayers, guidelines governing levies should be drafted and enforced.

Many seizures which the IRS makes are totally unnecessary. Sometimes the value of the property seized is so small that the expenses involved in seizing and selling the property are greater than their sale price. These small seizures are only valuable as harassment tactics, and should therefore be discounted.

My last major recommendation is for the creation of a new position in the Internal Revenue hierarchy. A new Office of Ombudsman should be maintained in the IRS. This Ombudsman should be a political appointee of the President, and his powers should include the right to intervene in any enforcement proceeding or activity when a taxpayer has made a petition to the Ombudsman, in the case of an alleged improper or illegal assessment, or an IRS violation of the Tax Code. As a political appointee, the Ombudsman would have the incentive to be responsive to taxpayers as opposed to career IRS employees, who are frequently judged on how "tough" they can be on taxpayers.

Of course, as I said at the beginning of my testimony, the best and most effective way to make life easier for the taxpayer is to move in the direction of tax simplification and tax abatement. A flat-rate type of approach is the most preferable way of doing this. Most of the IRS abuse problems would go away if Congress were to move in this direction.

However, IRS abuse can be controlled if Congress were to enact the changes to the IRS Code which I have just outlined and are contained in our book, The Power to Tax.

Mr. Chairman, I want to thank you for the opportunity to speak before your committee on the issue of efforts to reduce taxpayer burdens.

Senator **Grassley**. Has that point you made about the Ombudsman ever been discussed in the last couple of decades?

Mr. **Capozzi**. I think Jack would answer that better; he wrote the book.

Mr. **Wade**. I think what he was referring to, specifically, is there already is an Office of Ombudsman within the IRS, and the proposal is to make the Ombudsman a political appointee rather than a career IRS civil servant.

Senator **Grassley**. Is that your point, sir?

Mr. **Capozzi**. Yes, that's the point.

Mr. **Donohue**. Senator, the issue—if I might just comment for a second. We have a very fine person as Ombudsman. The only thing is she works for the Commissioner of IRS. So when you decide you are going to rule against the institution, you go in and tell your boss that you just have found against the actions of the organization that he runs.

Senator **Grassley**. All right.

During the Nixon administration he was outside the IRS, and so you would want to go back to that, is that right?

Mr. **Donohue**. I think that's right, sir. It is not for us to define exactly how to do it. The committee here and others in the Congress have great experience in that. The issue is very simple, though: Who is the person going to work for? And if he works for the guy in charge of the IRS, it's not very likely that he is going to be very independent.

Senator **Grassley**. I think we ought to be reminded of the fact that it was about that time, though, that the White House started using income tax investigation as a political tool.

Mr. **Donohue**. But when we are talking about a political appointee, we are not at all suggesting someone on the White House staff. There are many political appointees in this Government who had commissions in regulatory agencies and other organizations that are protected by the Congress. And we have in mind—at least we have in mind, Citizens Choice would have in mind—some independent auditor to whom the citizens, the taxpayers, could take their complaints when other avenues of redress are worked out in the IRS and there is nowhere else to go. It would keep people out of court; it would give us this third party that was discussed here on matters of seizure and other circumstances.

If you have a problem right now with the IRS, you have a serious difficulty in your own office. You start saying, "Well, how do we call up the IRS? We can call them up and tell them to look at it, but where do you go?" You have to tell a constituent that if they can't work it out they will have to go to court. Or we would say, "Go to the Ombudsman." And I go back to my fox in the chicken coop situation.

Senator **Grassley**. You know, speaking in regard to that from experience we have had, it is difficult to get the taxpayer to understand that. In fact, many a time I am sure that the taxpayer's intent in approaching us is that we can solve this problem for them, all we've got to do is pick up the phone and do it. I mean, that's implicit in what they said.

Mr. **Donohue**. Right. And the minute you try, you hear from the IRS that there is some effort on your part to influence their decision.

Senator **Grassley**. Well, we will have to look at the suggestion. There is surely nothing wrong with us looking over the historical approach to it—it has had a couple of different approaches—and seeing if there is anything better. And from that standpoint, I am glad that it was brought up.

I guess I would like to ask any or all of you how accurate you feel that taxpayer service on advice and assistance has been.

Mr. **Wade**. Senator, having been an IRS employee, about 9 years ago, in 1974, I was Online Supervisor to the Taxpayer Assistance Section in the Baileys Crossroads office. I am fully aware how difficult it is to provide accurate advice.

The IRS now has a training program about 5 or 6 weeks long for Taxpaver Service personnel, and basically they do the best they can with the kind of people that they are hiring.

Part of the problem I think is the low grade of the Taxpayer Service employees, and the fact that they may not have high intellectual skills. I think that the IRS could take another look at some of the hiring practices and try to raise the intelligence level of their employees; you would probably get a higher rate of response.

I know, from working Taxpayer Service, that early in the filing season when you have these people who are just recently trained and brought on, that you get a higher error rate at the beginning of the season than you do at the end of the season. And it has a lot to do with the experience of these people and whether or not they have been able to field these questions.

Also there is a great disparity, probably, in the level of expertise from the urban areas to the rural areas. You will find in the urban areas, for example, like in Washington, D.C., you get some tremendously technical questions—technical questions that, when I worked on this program, we used to get revenue agents with 20 years of experience to try to answer—the kind of questions that you would not necessarily get in the urban areas.

I think the IRS needs to recognize that there is a difference, and they need to pay more attention to the level of expertise and assistance that is provided in the urban areas, particularly in places like Washington, New York, San Francisco, Dallas, and the big cities.

Mr. **Donohue**. Senator, I think you have to sort of look at this in different groupings. The business community, large corporations particularly, can get binding rulings from the IRS. They send their lawyers around, and there is a process, as you know. And that works out. Even though you hire three good accounting firms and ask them the same question, they will give you different answers about how to interpret the IRS Code, but you can get an interpretation from the IRS. And I am not worried about them—they are big boys, and they can take care of themselves.

And I am not worried about the person who files the short form and puts down how much money they make—have you seen the one that says, "How much do you make? Please send it all."

I am worried about the middle-income taxpayer who is confused and who calls up and says, "How do I do this? Mama died this year, and I inherited her house," or, "What do I do because I sold my one batch of stock?" And it is very difficult to get a straight answer on that. One of the reasons is, it is very difficult to ask a straight question; because if you don't know what kind of a question to ask and how to pose it, you can confuse the person on the other end of the phone.

I think the IRS is making a lot of effort in that direction, but I think it is one of the reasons we ought to look at their budget. They can't go on on a continuing resolution. Every time you get a really good person in the IRS, a good accounting firm or a law firm or the Chamber will steal them; because you don't have to spend a lot of money to compete for the top folks. And I think we ought to look at getting them a few more good people. And that is one expenditure—we are fighting against Government expenditures, but that is one sound expenditure.

Senator GRASSLEY. When you say they are making a lot of progress, do you mean over the long term, very gradually, or because of changes in policy made recently?

Mr. DONOHUE. I think recent policy changes have taken this away from being a one-sided ballgame. It wasn't very long ago before you and others started these hearings and started working very hard on the matters of the compliance protection, that to say that the IRS could be arbitrary and capricious might be an understatement.

I think the IRS, under Commissioner Egger, who is a fine man, has been very, very careful to begin to try to address the problems of the compliance, because they realized that there are more of us than there are of them, and that they are losing the statistical battle, and that people are dropping out of the system. They are trying, therefore, to be more reasonable and look to the rights of the individual. They also are doing it because there are more individuals getting organized so that we are able to address these problems. I would give them an "A" for effort, and I would give them a "C" for performance. We are moving in the right direction, but they need some more resources.

Senator GRASSLEY. Well, is that "C" a better grade than you would have given the same agency 4 years ago?

Mr. DONOHUE. Definitely.

Mr. KEATING. Mr. Chairman, I would like to just concur with Mr. Wade's comments on the quality of the advice. I would also like to raise a disturbing issue—there really does seem to be a double standard in the quality of the advice given. There is one set given to corporations and very sophisticated individuals; but for the average individual it is very hard to figure out even how to write, and to whom, to obtain a private letter ruling. It is virtually impossible for the typical taxpayer.

There are no warnings in the IRS literature that say IRS telephone advice cannot be guaranteed. People have, on occasion been slapped with negligence penalties for following oral IRS advice. That may be understandable, if they called early in the season; nevertheless, I think we need to warn taxpayers that, although the advice is probably reasonable, there are occasions where it will be incorrect, and therefore cannot be guaranteed. This does not have to be a difficult thing to do. A simple warning in IRS publications or a recording played before you actually talk to an agent over the phone would suffice.

Senator **Grassley**. All right.

I would like to ask you whether or not the problem resolution program of IRS has been successful from your standpoint, and whether or not it gets adequate publicity.

Mr. **Donohue**. We just had a little advice from counsel who works on this all the time, and he said that he thinks that it has been more successful of late, and that in a lot of our mail and comments people have been surprised at how they have been treated by the IRS.

We would all agree it doesn't get enough publicity.

You have no idea, Senator, how continued hearings like this, and the debate on these issues in the public, and the willingness of late of the press to address it with more depth and interest has an effect on the Internal Revenue Service.

Senator **Grassley**. I am not sure I do know, but I'm glad to know. It sounds good.

Mr. **Donohue**. Well, I'm telling you, much like every other Government agency in this city, they read the Washington Post and the New York Times, and the other papers from around the country. If they find a continued interest by the Congress, by the administration, by representative groups such as ours around the country, they begin to be very, very careful to watch how they fulfill the mandate of the law and the regulation. People are very careful about things that get public scrutiny, and the more you do this I think the better we are.

I don't think Mr. Egger misses the point when he is up here more than he has been before, talking on these issues. Somebody has to write that testimony. Somebody has to go out and ask those questions. Somebody has to respond to the questions that you have been asking. And it is amazing what they find.

I think some of your other panelists here can give you chapter and verse on that. And I would just encourage you to charge on.

Senator **Grassley**. Anybody on the same point?

[No response]

Senator **Grassley**. All right.

I asked something along this line of the other two panels, whether or not the Paper Reduction Act discourages the IRS from requesting needless information.

Mr. **Donohue**. I will give you a personal experience. You are talking about paper reduction--one of our family members sent a pile of stuff like this on a sort of complicated issue. Fortunately, before it went, I said, "Make sure you make a copy." We sent the same stuff a second time, because it was lost.

But you have to be reasonable about this. It is so easy to say, "Oh, how incompetent!" If you ever went and looked at the mail that the IRS receives on a given day, at any time during the year, not to mention tax time, you need forklift trucks to move it around. We are talking about a paper blizzard from tens and tens of millions of people who pay taxes.

So when you are dealing with computer systems that are somewhat antiquated, when you are dealing with people that work 8 hours a day and take one file at a time by the number, you are going to have those kinds of problems. It is very, very important not to be taken away from the crucial point here by all the ancillary issues of "There are too many pieces of paper."

The point is that the taxpayer must have a feeling that the system is fair, equitable, reasonable, and responsive, and that they are not being handled by somebody who is going to deny them their rights and their protections. And we need to have some third party folks keeping an eye on that. We need to keep the pressure on the Service.

We need to do exactly what you are doing. But don't let them have you running off down the road looking at reducing paper by 10 percent instead of looking at getting those regulations written that passed in the law last time.

You ask the IRS what has happened to the requirement under the new law to advise those being audited of their rights, and they will tell you they are writing it up. So they ought to get on with it. They ought to get a new statement. They ought to have a statement, as David indicated, that the advice that is given on the telephone is not binding, that that person doesn't work for us anymore.

It is very important to keep an eye on the target here, and that is, the taxpayer is thinking seriously about whether to stay involved in the system.

Mr. KEATING. I would like to comment briefly on that.

It is hard to separate the total effect of increased paperwork caused by new tax legislation and its additional reporting requirements from efforts for form simplification, which reduces paperwork.

I think something that holds a lot of potential are safe harbor provisions. If you can just verify that you were actually doing something that day, you can forget about the rest of the paperwork. And I think that is very important. I would hope the IRS would move more quickly in that direction.

There is one form that really grates on me, though, and that is the form schedule SE for the self-employment tax. I would think that many direct sellers and other self employed persons don't have any farm or partnership income, and there is really no reason to have a schedule SE that has all those confusing questions in parts 1 and 2, along with the several paragraphs of instructions in form 1040. I think they can cut that form down considerably and save taxpayers much confusion. It is a very simple calculation, but you wouldn't know it by looking at the form and the instructions.

Senator GRASSLEY. Does the Paperwork Reduction Act hinder the IRS' ability to provide clear and direct guidance to taxpayers?

Mr. DONOHUE. Well, I think what David suggested, Senator, I don't think he is suggesting that.

Sometimes when I look at those instructions, specifically the one David mentioned, I think about putting together the children's toys at Christmas. I have long since abandoned the instructions and taken out on my own. And I think you do just as well.

What we really need is—I wouldn't let up on the paperwork reduction. If they can't say it in a page, somebody with a 10th grade education can't understand it.

Now, if we are talking about the complex regulations that tax business, with 7,000 pages of, you know, "Here's your chance to make your deal," we have another situation. But we are talking about the individual taxpayer, and it needs to be simple, and short, and understandable. And if it's not, people are not going to understand it; they are not going to comply with it; they are going to be frightened by it; and whenever they have a chance they are not going to send their money.

Senator **GRASSLEY**. Any further comment there?

[No response.]

Senator **GRASSLEY**. I believe that's all the questions I have. I want to thank you all for your participation and remind you, too, that there may be other members of the committee who will write to you. And if there is anything further that you have to submit, the record will be open for a time.

The meeting is adjourned.

[Whereupon, at 12:21 p.m., the hearing was concluded.]

[By direction of the chairman the following communications were made a part of the hearing record:]

H&R Block, Inc.
Corporate Headquarters
4410 Main Street
Kansas City, Missouri 64111
(816) 932-8413

Henry W. Bloch
President and
Chief Executive Officer

Statement of Henry W. Bloch
President of H & R Block, Inc.
for the Record of the Hearing
of the
Senate Finance Committee
May 20, 1983

Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to submit this written statement for the official record of your May 20, 1983, hearing on efforts to reduce taxpayer burdens.

As you know, a deduction for tax return preparation expenses is available to those taxpayers who file returns claiming itemized deductions. This encourages taxpayers to seek professional tax help, thereby reducing their burden in preparing their tax returns. But a similar tax assistance benefit is not available to those who do not itemize deductions -- usually lower income taxpayers and those who are least able to understand the tax laws. Millions of our clients view this as a glaring inequity.

A fair solution to this inequity -- while recognizing our governments' responsibility to help all taxpayers meet their tax responsibilities -- is to grant a small tax credit to all taxpayers for tax preparation expenses. Any costs exceeding the small credit should be deductible, as now allowed by those who itemize deductions.

It is by now universally recognized that it is vital to the health of the income tax system that it be perceived by all taxpayers (those with smaller incomes as well as those with larger incomes and those who understand the ever-more-complex law and those who don't understand it) as a system which has the fundamental objective of fairness and evenhanded treatment of all taxpayers. It is unjust and incomprehensible to the taxpayer who files the two-page Form 1040A or who files a Form 1040 but does not itemize, that he or she is not entitled to a tax benefit for the expenses incurred in having his or her return prepared by professional preparers.

Quite aside from the inequity of the situation, practical advantages to the government should result from an amendment to the Internal Revenue Code providing for such a benefit. Some, but not all, of the advantages would seem to be as follows:

1. The government is aware of the difficulties and high costs of administering its own tax assistance program. The provision for the new credit should encourage taxpayers to seek private sector assistance in lieu of visiting or telephoning offices of the Internal Revenue Service. This should help reduce the Internal Revenue Service taxpayer assistance budget and make more resources available for compliance, audit, collection and enforcement activities and for tax return processing work.

2. The amendment should help reduce some of the costs of printing and distributing forms and instructions since many private sector preparers do not utilize government forms. Unless requested by the taxpayer (by checking a box on the return) there would be no need to distribute the forms packages. A reminder card with the peel-off address label would suffice. A number of states have already recognized the potential savings in this area and adopted such a practice.

3. Assistance from qualified tax return preparers will help insure the preparation and filing of returns that generally are, and should continue to be, more accurate than those prepared by taxpayers themselves. A credit will encourage taxpayers to seek assistance from qualified preparers which should improve accuracy and thus the functioning of the entire system.

4. Such a credit and the subsequent encouragement to taxpayers to use qualified tax return preparers should have the additional result of more peace of mind to taxpayers that they have not under- or over-reported their tax obligations and that if and when audited, they would be accompanied by a qualified individual with supporting data.

5. Public confidence in the tax system would increase, especially on the part of the lower income taxpayers who do not understand the law and who are concerned with obtaining reliable advice but often cannot afford to do so. In any event, the IRS is regarded by many of these taxpayers as an enforcement agency, and to them information received from the IRS is therefore suspect. The only real choice for many taxpayers is a reliable tax return preparer.

6. The success of the American tax system is dependent to a great extent on voluntary compliance. Such voluntary compliance would be enhanced as a result of the adoption to this benefit with more revenue received by the government.

7. If tax withholding on interest and dividends becomes a fact, taxpayers will have heavier compliance burdens. The assistance of professional preparers should decrease the compliance burden of

taxpayers and result in fewer errors on returns filed, thus decreasing the IRS processing and compliance burden resulting from such withholding.

In summary, public policy reflected in the Internal Revenue Code for many years is intended to encourage the use of paid tax preparation assistance for itemizing taxpayers who are usually higher income taxpayers. The tax savings from such a policy until recently was worth as much as 70% of the fees paid to preparers and will still be worth as much as 50% under current law.

Such a policy should be applicable to all taxpayers. It may even be argued that from a public interest standpoint it is even more important to have the policy apply to lower income taxpayers since they are frequently the ones who find it difficult to understand tax laws, are uncertain about deductions and exemptions, are unable to deal with the forms themselves and can least afford to pay for tax preparation help. Millions of individuals file forms 1040A or 1040EZ and numerous others do not itemize deductions. They deserve the same benefit and incentive to seek competent tax preparation assistance from the private sector as the itemizing taxpayer.

A reduction in the tax burden for non-itemizing taxpayers and equal access to tax preparation assistance for all taxpayers would be best achieved by a tax credit for income tax preparation fees.

I respectfully request that you introduce a bill which would allow a $25 tax credit for everyone regardless of the tax form used with any expenses incurred for tax preparation fees over the $25 credit being allowed as a deduction for those who itemize deductions. This would help substantially the masses of taxpayers without giving any significant added benefit to those with high incomes.

I would be pleased to discuss this in greater detail with you or a member of your staff.

Very truly yours,

Henry W. Bloch

Henry W. Bloch

HWB:pv

STATEMENT OF THE IOWA FARM BUREAU FEDERATION
TO THE SENATE FINANCE SUBCOMMITTEE
ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE

EFFORTS TO REDUCE TAXPAYER BURDENS
HEARING DATE: MAY 20, 1983

The Iowa Farm Bureau Federation is a general farm organization with a membership exceeding 149,000 families. Farm Bureau is a voluntary organization which is united for the purpose of analyzing common problems and formulating action to achieve economic opportunity and social advancement. The Iowa Farm Bureau offers a number of services to its members in order to achieve these goals. In response to the members' growing need for accurate recordkeeping, Farm Bureau created a farm records division in 1966 to help members prepare and maintain needed documents.

Farming combines traditionally separate industrial functions. The farmer is both labor and management. Crucial to his or her managerial role is the ability to keep detailed, accurate records. At its inception in 1966, Iowa Farm Bureau's farm records division assisted 504 farmers/taxpayers. In 1982, this number has grown to 3,264. In large part, this increase is due to the increasingly complex tax statutes, regulations and forms. In order to minimize tax liability, farmers as well as all individuals, must maintain a plethora of records.

Non-self-employed taxpayers with little dividend or interest income have few forms or schedules to submit when completing the form 1040. However, a simple farm transaction, for example — the sale of a cow purchased for breeding purposes and held more than two years — may involve as many as seven separate steps with reporting requirements for each.

Step 1: The sale must be reported on form 4797 (sale of items used in business).

Step 2: The calculations on form 4797 must then be transferred to schedule D (capital gains and losses).

Step 3: The figures then must be transferred to form 1040.

Step 4: Since the cow was a purchased cow, the farmer must complete form 4255 (investment credit recapture). Then this figure would be transferred to the 1040.

Step 5: The amount of depreciation on the cow must be indicated on form 4562.

Step 6: This depreciation figure then goes to schedule F (farm income and expenses) and then the schedule F figure is transferred again to form 1040.

Step 7: If the farmer sells several cows in a year and has substantial capital gains, the farmer may have to complete form 6251 (alternative minimum tax) with the results of these calculations then transferred to schedule 1040.

As you can see from this example, farmers still are overly burdened by the income tax reporting system. Our farm records division reports that their paper work has not been reduced; and in fact, the major result of the Paper Works Reduction Act is that the forms are now accompanied by a paragraph stating that the information is necessary to carry out the Internal Revenue laws of the United States.

It is difficult at best to separate form from substance when the subject is taxes. The IRS is in an unenviable position of gleaning legislative intent from acts of Congress, and proposing workable and understandable forms to implement the law. As tax laws become more complex, thereby requiring the IRS to administratively develop forms and schedules, the ability of taxpayers to comprehend the regulations diminishes arithmetically, more likely geometrically. Given our voluntary tax reporting system, this is a most troubling trend. The incentives to abuse the system may be linked to complex statutory changes, which the IRS has little choice but to implement. Perhaps it is time to not only examine IRS forms, but also the laws that spawned the forms.

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